

**CITY OF HARLINGEN  
WATERWORKS SYSTEM  
FINANCIAL STATEMENTS  
AND  
INDEPENDENT AUDITORS' REPORT**

**For the Fiscal Years Ended  
September 30, 2017 and 2016**

**Prepared by:**

**Finance Department  
Kathern Davidson, Finance Director**

**CITY OF HARLINGEN WATERWORKS SYSTEM  
ANNUAL FINANCIAL REPORT**

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## CITY OF HARLINGEN WATERWORKS SYSTEM

March 28, 2018

Utility Board of Trustees,  
Members of the City Commission  
Citizens of the City of Harlingen, Texas

Management is pleased to submit the annual financial report of the City of Harlingen, Texas Waterworks System (the "System") for the fiscal year ended September 30, 2017.

This report is published to provide the citizens, City Commission, Utility Board of Trustees, the System staff, bondholders, and other interested parties detailed information concerning the financial condition of the System. Responsibility for both the accuracy of the presented data and the completeness and fairness of the presentation, including all disclosures, rests with the System.

To the best of our knowledge and belief the data is accurate in all material aspects, and is organized in a manner designed to fairly present the financial position and results of operations of the System as measured by its financial activity. We also believe that all disclosures necessary to enable the reader to gain the maximum understanding of the System's financial affairs have been included.

The City Charter requires an annual audit of the financial records and transactions of the System by an independent auditor.

This report is comprised of three sections: Introductory, Financial and Statistical. The Introductory Section includes this transmittal letter, a listing of the principal System officials, and an organizational chart of the System. The Financial Section contains the Independent Auditors' Report on the basic financial statements, Management's Discussion and Analysis ("MD&A"), the basic financial statements, with related notes and supplemental schedules. The MD&A is a narrative introduction, overview, and analysis to accompany the basic financial statements. This letter of transmittal is designed to complement the MD&A and should be read in conjunction therewith. The System's MD&A can be found immediately following the Independent Auditors' Report. The Statistical Section provides financial and demographic information, usually presented on a multi-year basis that is relevant to a financial statement reader.

The Financial Section described above is prepared in accordance with generally accepted accounting principles for governments as prescribed by the Governmental Accounting Standards Board ("GASB") and other professional associations, as applicable.

The City of Harlingen (the "City") is located in Cameron County in the center of the Rio Grande Valley, at the southern tip of Texas. The City covers approximately 32 square miles, and has an estimated population of 66,415. The City is a political subdivision and

municipal corporation of the State, duly organized and existing under the laws of the State, including the City's Home Rule Charter. The City was incorporated in 1910, and first adopted its Home Rule Charter in 1927. The City operates under a Commission/Manager form of government. The System provides water treatment and distribution services and wastewater collection, treatment and disposal services for the citizens of the City and, to areas beyond its corporate boundaries pursuant to a Certificate of Convenience and Necessity, issued by the Texas Commission on Environmental Quality. The System is owned by the City, but by Charter Amendment, is operated under a Utility Board of Trustees (the "Board"). The Board is responsible for the management and operation of the System. The City Commission appoints the members of the Board; approves the retail rates and wholesale contracts of the System; approves the System's annual budget; and authorizes the issuance of debt.

The System's accounting records are maintained on an accrual basis. In developing and maintaining the System's accounting system, consideration is given to the adequacy of the internal control structure. Internal accounting controls are designed to provide reasonable, but not absolute assurance regarding: (1) the safeguarding of assets against loss from unauthorized use or disposition; and (2) the reliability of financial records for preparing financial statements and maintaining accountability for assets. The concept of reasonable assurance recognizes that the cost of a control should not exceed the benefits likely to be derived; and the evaluation of costs and benefits requires estimates and judgments by management. All internal accounting control evaluations occur within the above framework. We believe that the System's internal accounting controls adequately safeguard assets and provide reasonable assurance of proper recording of financial transactions.

The preparation of this report would not have been accomplished without the efforts and dedicated services of the staff of the Finance Department. We would like to express our appreciation to all members of the department who assisted in the preparation of this report. Credit also must be given to the Utility Board of Trustees for their interest and support in planning and conducting the financial affairs of the System in a responsible and professional manner.

Respectfully submitted,



Timothy E. Skoglund, P.E.  
General Manager



Kathern Davidson  
Finance Director



**CITY OF HARLINGEN WATERWORKS SYSTEM**

**ANNUAL FINANCIAL REPORT**

**SEPTEMBER 30, 2017**

**UTILITY BOARD OF TRUSTEES**

**Officers**

**Joshua Fields, Chairman** **May 2019**

**Michael Garza, Vice-Chairman** **May 2020**

**Members**

**Kevin Campbell** **May 2021**

**Curtis Bonner** **May 2018**

**Michael Murphy** **May 2019**

**Ex-Officio Members**

**Chris Boswell, Mayor**

**Dan Serna, City Manager**

**General Manager**

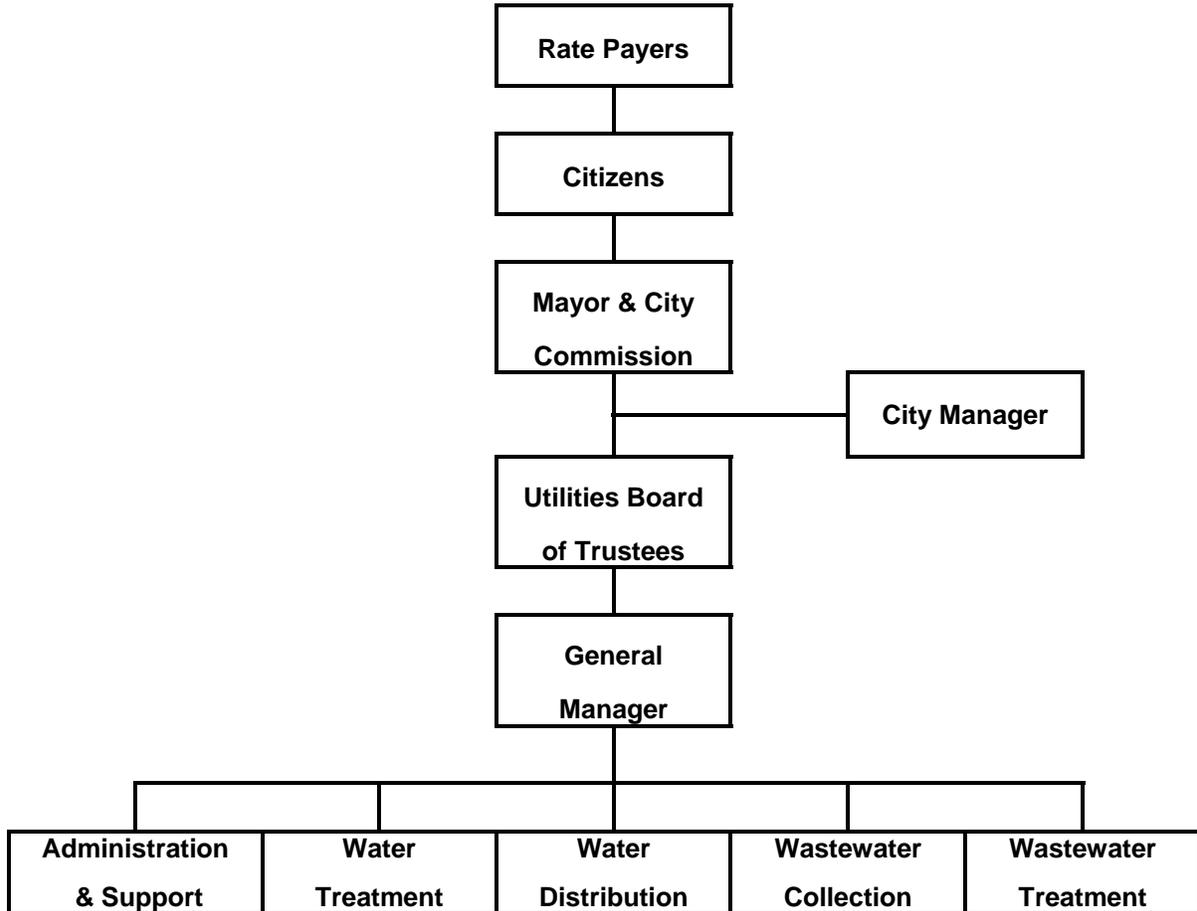
**Timothy E. Skoglund, P.E.**

**CITY OF HARLINGEN WATERWORKS SYSTEM**

**ANNUAL FINANCIAL REPORT**

**SEPTEMBER 30, 2017**

**ORGANIZATIONAL CHART**



## INDEPENDENT AUDITORS' REPORT

To the City of Harlingen  
Waterworks System Board of Trustees

### Report on the Financial Statements

We have audited the accompanying financial statements of the City of Harlingen Waterworks System, a component unit of the City of Harlingen, Texas, as of and for the years ended September 30, 2017 and 2016 and the related notes to the financial statements, as listed in the table of contents.

#### *Management's Responsibility for the Financial Statements*

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

#### *Auditors' Responsibility*

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

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## ***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the City of Harlingen Waterworks System, as of September 30, 2017 and 2016 and the respective changes in its financial position and cash flows thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.

## ***Other Matters***

### *Required Supplementary Information*

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and required supplementary information on pages 13 through 21 and pages 51 through 55 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

### *Supplementary and Other Information*

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the City of Harlingen Waterworks System's basic financial statements. The introductory section, other supplementary information section and statistical section, as listed in the accompanying table of contents, are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The other supplementary information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the other supplementary information is fairly stated, in all material respects in relation to the basic financial statements as a whole.

The introductory section and statistical section have not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

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**Other Reporting Required by *Government Auditing Standards***

In accordance with *Government Auditing Standards*, we have also issued our report dated March 28, 2018, on our consideration of the City of Harlingen Waterworks System's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the City of Harlingen Waterworks System's internal control over financial reporting and compliance.

*Carr, Riggs & Ingram, L.L.C.*

Harlingen, Texas  
March 28, 2018

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**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Management's Discussion and Analysis**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

As management of the City of Harlingen Waterworks System (the "System"), we offer readers of the System's financial statements this narrative overview and analysis of the financial performance of the System for the fiscal years ended September 30, 2017 and 2016. We encourage readers to consider the information presented here in conjunction with the System's audited financial statements, which begin on page 22.

**OVERVIEW OF THE FINANCIAL STATEMENTS**

The System is a component unit of the City of Harlingen, Texas. These statements are included in the comprehensive annual financial report of the City. As a proprietary type component unit of the City, the System operates in a manner similar to a private business enterprise. The intent of the governing body of the City of Harlingen is for the costs (expenses, including depreciation) of providing goods or services to the general public on a continuing basis, to be financed or recovered primarily through user charges. This report consists of the basic financial statements of the System: (a) the Statement of Net Position; (b) the Statement of Revenues, Expenses, and Changes in Net Position; (c) the Statement of Cash Flows; and (d) the Notes to the Financial Statements. These statements provide a broad overview of the results of the System's operations.

The Statement of Net Position presents information on all of the System's assets and deferred outflows of resources, liabilities and deferred inflows of resources, with the difference reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the System is improving or deteriorating.

The Statement of Revenues, Expenses and Changes in Net Position presents information showing how the System's net position changed during the most recent fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

The Statement of Cash Flows reports cash flows in three separate categories (operating, capital and related financing, and investing).

The basic financial statements can be found on pages 22-26 of this report.

Notes to the Financial Statements provide additional information that is essential to a full understanding of the data provided in the aforementioned statements. The notes to the financial statements can be found on pages 27-50 of this report.

In addition to the basic financial statements and accompanying notes, this report also presents certain *required supplementary information*, concerning the System's progress in funding its obligation to provide pension benefits and health care benefits to employees who retire from the System, which can be found on page 51-55 of this report. Other supplementary information presented on pages 56-59 provides detailed revenues and expenses for the System's two operational departments, water and wastewater; for the current and previous fiscal years and a budgetary comparison schedule.

The Statistical Section includes financial and demographic information, usually presented on a multi-year basis that is relevant to a financial statement reader, is presented on pages 60-68.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Management's Discussion and Analysis, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**FINANCIAL HIGHLIGHTS**

A summary of the System's net position is presented below together with relevant comments and information:

**SUMMARY OF NET POSITION**  
**as of September 30,**

<u>Assets</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>
Current assets	\$ 23,327,564	\$ 18,417,798	\$ 15,802,931
Current restricted assets	9,752,429	11,880,802	15,177,216
Noncurrent assets:			
Net pension asset	-	-	1,953,444
Capital assets	70,661,842	69,811,864	67,536,344
Total assets	<u>103,741,835</u>	<u>100,110,464</u>	<u>100,469,935</u>
 <u>Deferred Outflows of Resources</u>			
Deferred amount on debt refunding	269,324	337,810	403,009
Deferred pension related outflows	1,543,195	1,988,470	271,954
Total deferred outflows of resources	<u>1,812,519</u>	<u>2,326,280</u>	<u>674,963</u>
 <u>Liabilities</u>			
Current liabilities	2,974,370	3,376,973	2,132,733
Current liabilities payable from restricted assets	622,180	602,118	380,446
Long term debt	22,348,939	23,856,169	25,341,003
Net retiree health care plan obligation	3,840,067	3,542,478	3,205,507
Net pension obligation	323,981	193,753	-
Customer deposits	2,107,602	1,885,000	1,600,000
Other noncurrent liabilities	190,817	233,000	200,000
Total liabilities	<u>32,407,956</u>	<u>33,689,491</u>	<u>32,859,689</u>
 <u>Deferred Inflows of Resources</u>			
Deferred pension related inflows	<u>56,456</u>	<u>93,042</u>	<u>130,558</u>
 <u>Net Position</u>			
Net investment in capital assets	50,579,546	51,415,795	54,124,539
Restricted	8,185,404	11,095,359	3,413,163
Unrestricted	14,324,992	6,143,057	10,616,949
Total net position	<u>\$ 73,089,942</u>	<u>\$ 68,654,211</u>	<u>\$ 68,154,651</u>

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Management's Discussion and Analysis, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**FINANCIAL ANALYSIS**

The assets and deferred outflows of the System exceeded its liabilities and deferred inflows at the close of the most recent fiscal year by \$73,089,942, an increase of \$4,435,731 from the previous year's balance.

The largest portion of the System's net position, \$50,579,546 (69.2%) reflects its investment in capital assets (land, water rights, buildings, machinery, equipment, and water and wastewater system improvements) less any related debt used to acquire those assets that is still outstanding. The System uses these capital assets to provide services to its customers. Consequently, the assets are not available for future spending. Although the System's investment in capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate the liabilities. An additional portion of the System's net position \$8,185,404 (11.2%), represents resources subject to external restrictions on how they may be used. The remaining balance of unrestricted net position \$14,324,992 (19.6%) may be used to meet the System's ongoing obligations to customers and creditors.

For the fiscal year ended September 30, 2017, the System's total net position increased by \$4,435,731. The factors in this increase include a decrease in the investment in capital assets, net of related debt of \$836,249; a decrease in restricted net position of \$2,909,955; and an increase in unrestricted net position of \$8,181,935.

The System added \$4,517,700 in capital assets and accepted ownership of \$432,882 in infrastructure contributed by developers in fiscal year 2017. These additions were partially offset by asset retirements in the amount of \$1,558,274 and depreciation for the fiscal year. The net of those transactions resulted in the carrying value of the System's capital assets to increase by \$849,978. The System's investment in capital assets is reported net of related outstanding debt. Therefore, the use of bond proceeds to acquire assets, and the retirement of debt both affect the valuation. In fiscal year 2017, the System spent \$3,171,061 in debt proceeds on capital improvements; and, the net carrying value of outstanding debt was reduced by \$1,484,834, resulting in an increase in the outstanding debt related to capital assets of \$1,686,227.

The \$2,909,955 decrease in restricted net position reflects the use of debt proceeds in the amount of \$3,171,061 to fund capital improvements. Funds restricted for the payment of principal and interest on debt increased by \$20,755. In 2017, impact fee, front-footage fee, and tie-in-charge revenues restricted for expansion and maintenance of infrastructure increased by \$779,268. In accordance with GASB Statement No. 68, the System includes its net pension related deferred outflows, deferred inflows, and net pension obligation in the calculation of the System's position. From 2016 to 2017, the decrease in restricted net position related to the System's pension obligation is \$538,917.

The System's unrestricted net position increase of \$8,181,935 is primarily due to the System's increase in revenues and use of debt proceeds to fund capital improvements, in lieu of utilizing funds derived from operations.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Management's Discussion and Analysis, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**Revenues**

Fiscal year 2017 customer fees and charges increased a total of \$2,054,180 (10.6%) in comparison to the previous year.

Retail water sales revenue increased by \$1,079,948 (20.25%) over fiscal year 2016 levels. Approximately \$533,000 (10%) of the increase can be attributed to the dry weather conditions in the service area in fiscal year 2017. From October 2014 through March 2017, the number of gallons of water included in the customer "base" water charge was reduced by 100 gallons per month, eliminating all water included in the customers' base fee. This has resulted in additional water revenue of approximately \$186,000 (4%) in fiscal 2015, \$635,000 (15%) in fiscal year 2016, and \$547,000 (10.25%) in fiscal year 2017. Fiscal year 2016 retail water service revenue of \$5,331,929 reflected an increase of \$1,108,114 (26.2%) over fiscal year 2015 levels. Wholesale water sales to local water providers increased by \$122,485 (25.3%) to \$605,942 in fiscal year 2017. Wholesale water sales revenue in fiscal year 2016 was only slightly higher than that of the previous year, with total revenue increasing \$4,859 (1.5%) over revenue of \$478,598 in 2015. Total water operating revenues increased by \$1,276,549 (13.7%) and \$1,083,699 (13.1%) in fiscal years 2017 and 2016, respectively.

Wastewater "base" customer charges increased \$307,622 (22.5%), \$295,804 (27.64%) in fiscal years 2017 and 2016, respectively. Beginning in November 2014, the wastewater base customer charge has been increased by \$0.10 per month, resulting in approximately \$290,000 in additional revenue in both 2017 and 2016. The 2017 and 2016 increases in water sales volume resulted in increases in wastewater billing, although in a lesser amounts. Wastewater service revenue increased by \$444,926 (5.74%) in 2017, and \$354,024 (4.78%) in 2016. For the 2017 fiscal year, total wastewater operating revenues increased by \$777,631 (7.7%).

As market rates increased, fiscal year 2017 investment earnings increased by \$88,784 (75.6%) to \$206,280; and \$54,636 (115.05%) to \$117,496 in fiscal year 2016. Fiscal year 2017 average invested balance of \$28,004,679 earned a rate of return of 0.73% while the fiscal year 2016 average invested balance of \$28,420,788 earned a rate of return of 0.41%; in comparison to the 2015 rate of return of 0.27% on the average invested balance of \$20,126,031.

Impact fee revenue of \$768,230 reflects an increase of \$303,854 (65.4%) over fiscal year 2016 revenues of \$464,376. Impact fees for residential service increased by 36%, while commercial impact fees increased by 217% in fiscal year 2017. Fiscal year 2016 impact fee revenue increased by only \$15,987 (3.57%) over fiscal year 2015 revenue of \$448,389. The average annual impact fee revenue for the previous four-year period (2016-2013) has been \$531,418. Fiscal year 2017 revenue is 44.6% above the four-year average, reflecting moderately higher than normal system growth.

Capital contributions of water and wastewater service lines for the 2017 fiscal year totaled \$432,882, an increase of 97.2% over 2016 fiscal year contributions of \$219,410, and within \$65,030 of the \$497,912 capital contributions in fiscal year 2015.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Management's Discussion and Analysis, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**Expenses**

Fiscal year 2017 operating expenses of \$18,301,951 represent a decrease of \$1,388,709 (7.05%) in relation to 2016 operating expenses of \$19,690,660. With the exception of a \$124,396 (1.55%) increase in personnel services expenses, all other categories of operating expenses decreased in comparison to fiscal year 2016 levels. In relation to expenses incurred in fiscal year 2015, fiscal year 2016 expenses were \$811,185 (4.3%) higher.

The 2017 budget included funding for an annual wage increase of \$1,200 for all employees, and three additional positions in Water operations, an increase of \$265,493. However, personnel services expenses totaled \$8,175,686, an increase of only \$124,396 (1.55%) in comparison to fiscal year 2016 expenses. Employee wages and related benefits and employment taxes decreased by \$136,138 (1.7%); retiree health care expense decreased by \$45,024 (7.6%); pension expense increased by \$193,609 (42.9%); and, the amount of wages capitalized decreased by \$111,949 (20.3%). Personnel services expenses had increased by \$819,519 (11.33%) to \$8,051,290 in fiscal year 2016. In 2016, six new positions were added in operations, at a cost of approximately \$247,000. In addition, pension expense in fiscal year 2016 was \$437,129 higher than pension expense in fiscal year 2015. In both 2016 and 2015, System employees received cost-of-living pay increases of \$1,200 annually, increasing expenses by approximately \$185,000 each year.

Contractual services expenses decreased by \$184,765 (5.3%) to \$3,274,701 in fiscal 2017. This reduction in expenses is primarily due to reduced electrical consumption at the new wastewater treatment plant. Fiscal year 2016 contractual services expenses of \$3,459,466 represented an increase of \$44,846 (1.31%) when compared to fiscal year 2015 expenses.

Supplies and maintenance expenses totaled \$2,886,769, a decrease of \$50,445 (1.7%) in fiscal year 2017. The reduction was realized in water and wastewater treatment chemical expenses. Changes in the types and amounts of chemicals used in the treatment processes created the savings. Supplies and maintenance expenses increased a mere \$6,648 (0.23%) in 2016, after a decrease of \$154,475 (5%) to \$2,930,566 in fiscal year 2015.

Fiscal year 2017 "Other" expenses totaled \$141,543, a reduction of \$98,922 (41.1%) in comparison to 2016 expenses of \$240,465. The most significant expense reduction was due to outsourcing customer bank card payment processing. This move resulted in savings in the amount of \$81,906 in fiscal year 2017. Expenses increased in 2016 by \$16,142 (7.20%) over fiscal year 2015 expenses of \$224,323. Merchant services fees and charges for bank card payment processing increased \$12,169 (11.0%) in fiscal year 2016, as the number of transactions increased throughout the year. The remainder of the increase was attributed to increased training and licensing expenses for operations staff.

Depreciation expense reflects a significant reduction in fiscal year 2017. Total depreciation expense in fiscal year 2017 is \$3,823,252, a decrease of \$1,178,973 (23.6%). The determination was made that water and wastewater mains have a longer expected service life than was previously estimated; resulting in the assets being depreciated too rapidly. The estimated service lives of water and wastewater mains were adjusted to more accurately reflect the currently anticipated useful lives. The increase in the service life of the assets has resulted in decreased depreciation expense over the remaining life of the assets. Depreciation expense was \$5,002,225 and \$5,078,195 in fiscal years 2016 and 2015, respectively.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Management's Discussion and Analysis, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

In fiscal year 2017, interest and amortization expense increased by \$41,563 (6.8%) to \$656,446. A reduction in capitalized interest combined with a reduction in interest on outstanding debt resulted in this expense reduction. Interest expense in fiscal 2016 decreased by \$395,296 due to an increase in capitalized interest and a reduction in interest on outstanding debt. Fiscal year 2015 interest expense was elevated by the payment of expenses associated with the issuance of the 2015 bonds.

**CHANGES IN NET POSITION**

	2017	2016	2015
Operating revenues	\$ 21,477,457	\$ 19,423,277	\$ 17,584,357
Operating expenses	18,301,951	19,690,660	18,879,475
Operating income (loss)	<u>3,175,506</u>	<u>(267,383)</u>	<u>(1,295,118)</u>
Non-operating revenues:			
Impact fees	768,230	464,376	448,389
Investment earnings	206,280	117,496	54,636
Other	509,279	580,544	683,260
Total non-operating revenues	<u>1,483,789</u>	<u>1,162,416</u>	<u>1,186,285</u>
Non-operating expenses:			
Interest expense and amortization	<u>656,446</u>	<u>614,883</u>	<u>1,010,179</u>
Change in net position before contributions	<u>4,002,849</u>	<u>280,150</u>	<u>(1,119,012)</u>
Capital contributions	<u>432,882</u>	<u>219,410</u>	<u>497,912</u>
Change in net position	<u>\$ 4,435,731</u>	<u>\$ 499,560</u>	<u>\$ (621,100)</u>

**CAPITAL ASSETS**

The value of the System's capital assets increased by \$849,978 and \$2,275,520 to \$70,661,842 and \$69,811,864 (net of accumulated depreciation) in fiscal years 2017 and 2016, respectively. This investment in capital assets includes land, water rights, buildings, machinery and equipment, and system improvements.

Fiscal year 2017 asset acquisitions totaled \$4,950,582, including \$432,882 in contributed assets. Asset retirements totaled \$1,558,274. The net accumulated depreciation on capital assets increased \$2,542,330. Total depreciation expense for the year 2017 of \$3,823,252 was offset by \$1,280,922 of accumulated depreciation on assets retired throughout the year.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Management's Discussion and Analysis, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

Significant capital asset events during the current fiscal year included the following:

- Completed construction of Phase II of the new Wastewater Treatment Plant – FY 2017 cost: \$1,581,115; Project-to-date cost: \$12,961,350
- Construction of 6,300 feet of 15 inch wastewater main on Spur 54 – FY 2017 cost: \$1,106,090
- Construction of lift station #55B on Spur 54 – FY 2017 cost: \$172,769
- Pipe-burst 1,850 feet of 15 inch wastewater main on New Hampshire – FY 2017 cost: \$399,326
- Purchased a utility tractor at a cost of \$111,977
- Purchased a used boom truck at a cost of \$176,080

Additional information on the City of Harlingen Waterworks System's capital assets can be found in note 5 on page 36 of this report.

**SCHEDULE OF CAPITAL ASSETS**  
as of September 30

	2017	2016	2015
Water rights	\$ 5,423,369	\$ 5,423,369	\$ 5,423,369
Land	1,208,953	1,202,089	1,189,507
Construction in progress	3,209,690	10,692,042	4,997,226
Water infrastructure	83,125,321	82,796,853	81,842,522
Wastewater infrastructure	84,068,166	73,922,946	73,595,631
Other buildings and equipment	4,549,269	4,372,568	4,325,970
Vehicles	3,189,456	2,972,049	2,834,751
Total capital assets	<u>184,774,224</u>	<u>181,381,916</u>	<u>174,208,976</u>
Less accumulated depreciation	<u>(114,112,382)</u>	<u>(111,570,052)</u>	<u>(106,672,632)</u>
Capital assets net of depreciation	<u>\$ 70,661,842</u>	<u>\$ 69,811,864</u>	<u>\$ 67,536,344</u>

**DEBT ADMINISTRATION**

At the end of the current fiscal year, the System had total bonded debt outstanding of \$23,685,000 with unamortized premiums and discounts of \$171,169 for net total debt of \$23,856,169. The debt is secured by a pledge of the revenues of the water and wastewater systems. The System retired \$1,455,000 in outstanding bonds in fiscal year 2017.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Management's Discussion and Analysis, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

On August 27, 2015 in conjunction with the issuance of the Series 2015A and Series 2015B bonds, the System's outstanding bonds were rated Aa2 by Moody's Investors Service, with a negative outlook; and AA- by Standard & Poor's with a stable outlook.

On July 17, 2017, Moody's Investors Service affirmed the Aa2 rating of the System's outstanding bonds, and revised the outlook to stable.

Additional information on the System's long term debt can be found in notes 8 and 9 on pages 38-40 of this report.

**As of September 30,**

<u>Revenue Bonds</u>	<u>2017</u>	<u>2016</u>	<u>2015</u>
Current portion	\$ 1,507,230	\$ 1,484,834	\$ 352,258
Long-term portion	22,348,939	23,856,169	25,341,003

The System does not plan to issue additional debt in the foreseeable future.

**FISCAL YEAR 2018 BUDGET AND RATES**

In October 2014, the System began eliminating the 3,000 gallons of water commodity from the water base service rate. Over the next 30 months, the amount of water included in the monthly base rate has been reduced by 100 gallons per month. This practice continued through March 2017, after which, no water commodity has been included in the monthly base service rate. Additionally, beginning in November 2014, the sewer base rate has been increased by \$0.10 per month. This will continue through March, 2018. As of October 1, 2017, the sewer base rate was \$5.78 per customer, per month.

The fiscal year 2018 operating revenue budget was developed using the average consumption over the most recent five-year period, and reflects 3.6% decrease when compared to operating revenue recognized in FY 2017. Fiscal year 2018 customer fees and charges were budgeted at \$20,696,000.

A decrease of \$800,598 in operating expenses was approved in the fiscal year 2018 budget. The addition of two positions, a 2% annual cost-of-living increase, and a 2% merit pay allocation increased the personnel services budget by \$356,202. The budget for contractual services was decreased by \$354,150, reflecting significant decreases in power consumption and energy rates. The supplies and maintenance category of expenses reflects an increase of \$161,450 as additional funding was budgeted for wastewater collection system maintenance. The "other" category of expenses decreased by \$114,100, reflecting the outsourcing of bank card payment processing. Depreciation expense decreased by \$850,000 due to the revision of the estimated service life of system infrastructure.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Management's Discussion and Analysis, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**REQUESTS FOR INFORMATION**

This financial report is designed to provide a general overview of the City of Harlingen Waterworks System's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Finance Director, 134 East Van Buren, Harlingen, Texas, 78550.

# **FINANCIAL STATEMENTS**

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Statements of Net Position**  
**As of September 30,**

	<b>2017</b>	<b>2016</b>
<b>ASSETS</b>		
<b>Current Assets</b>		
Cash and cash equivalents	\$ 11,249,565	\$ 9,906,621
Investments	9,388,827	5,896,408
Accounts receivable, net of allowance for uncollectible	2,241,649	2,112,871
Interest receivable	39,239	3,737
Inventories	393,825	390,004
Prepaid items	14,459	108,157
<b>Restricted assets</b>		
Cash and cash equivalents	4,121,962	4,236,075
Investments	5,630,467	7,644,727
Total current assets	33,079,993	30,298,600
<b>Noncurrent Assets</b>		
Capital assets:		
Capital assets, not being depreciated:		
Land	1,208,953	1,202,089
Construction in progress	3,209,690	10,692,042
Water rights	5,423,369	5,423,369
Other capital assets, net of accumulated depreciation	60,819,830	52,494,364
Total capital assets	70,661,842	69,811,864
Total noncurrent assets	70,661,842	69,811,864
Total assets	\$ 103,741,835	\$ 100,110,464
<b>DEFERRED OUTFLOWS OF RESOURCES</b>		
Deferred amount on debt refunding	\$ 269,324	\$ 337,810
Pension contributions after measurement date	80,713	26,964
Difference in projected and actual earnings on pension assets	1,047,861	1,416,121
Difference in expected and actual pension experience	414,621	545,385
Total deferred outflows of resources	\$ 1,812,519	\$ 2,326,280

The notes to the financial statements are an integral part of these statements.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Statements of Net Position - continued**  
**As of September 30,**

	<b>2017</b>	<b>2016</b>
<b>LIABILITIES</b>		
<b>Current Liabilities</b>		
Accounts payable	\$ 438,380	\$ 502,574
Due to primary government	111,801	143,059
Other liabilities	344,959	702,989
Compensated absences - current	572,000	543,517
Revenue bonds - current	1,507,230	1,484,834
Payable from restricted assets:		
Accrued interest	322,180	334,305
Customer deposits - current	300,000	267,813
Total current liabilities	3,596,550	3,979,091
<b>Noncurrent Liabilities</b>		
Revenue bonds payable (net of unamortized premiums and discounts)	22,348,939	23,856,169
Compensated absences	190,817	233,000
Net retiree health care plan obligation	3,840,067	3,542,478
Net pension obligation	323,981	193,753
Payable from restricted assets:		
Customer Deposits	2,107,602	1,885,000
Total noncurrent liabilities	28,811,406	29,710,400
Total liabilities	\$ 32,407,956	\$ 33,689,491
<b>DEFERRED INFLOWS OF RESOURCES</b>		
Difference in expected and actual earnings on pension assets	\$ 930	\$ -
Difference in expected and actual pension experience	55,526	93,042
Total deferred inflows of resources	\$ 56,456	\$ 93,042
<b>NET POSITION</b>		
Net investment in capital assets	50,579,546	51,415,795
Restricted	8,185,404	11,095,359
Unrestricted	14,324,992	6,143,057
Total net position	\$ 73,089,942	\$ 68,654,211

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Statements of Revenues, Expenses and Changes in Net Position**  
**For the Fiscal Years Ended of September 30,**

	<u>2017</u>	<u>2016</u>
<b>Operating Revenues</b>		
Customer fees and charges	\$ 21,477,457	\$ 19,423,277
<b>Operating Expenses</b>		
Personnel services	8,175,686	8,051,290
Contractual services	3,274,701	3,459,466
Supplies and maintenance	2,886,769	2,937,214
Other	141,543	240,465
Depreciation	3,823,252	5,002,225
Total operating expenses	<u>18,301,951</u>	<u>19,690,660</u>
<b>Operating Income (Loss)</b>	<u>3,175,506</u>	<u>(267,383)</u>
<b>Non-Operating Revenues</b>		
Impact fees	768,230	464,376
Investment earnings	206,280	117,496
Other	509,279	580,544
Total non-operating revenues	<u>1,483,789</u>	<u>1,162,416</u>
<b>Non-Operating Expenses</b>		
Interest and amortization expense	<u>656,446</u>	<u>614,883</u>
<b>Change in Net Position before Contributions</b>	4,002,849	280,150
Capital Contributions	<u>432,882</u>	<u>219,410</u>
<b>Change in Net Position</b>	4,435,731	499,560
Net Position - Beginning Year	<u>68,654,211</u>	<u>68,154,651</u>
<b>Net Position - End of Year</b>	<u>\$ 73,089,942</u>	<u>\$ 68,654,211</u>

The notes to the financial statements are an integral part of these statements.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Statements of Cash Flows**  
For the Fiscal Years Ended September 30,

	<b>2017</b>	<b>2016</b>
<b>Cash Flows From Operating Activities</b>		
Receipts from customers	\$ 22,319,814	\$ 20,308,837
Payments to suppliers	(6,466,765)	(6,714,105)
Payments to or on behalf of employees	(7,281,538)	(7,365,573)
Net cash provided by operating activities	8,571,511	6,229,159
 <b>Cash Flows From Capital and Related</b>		
<b>Financing Activities</b>		
Acquisition and construction of capital assets	(4,757,010)	(6,964,121)
Proceeds from impact fees	768,230	464,376
Principal paid on revenue bonds	(1,455,000)	(320,000)
Interest and fees paid on revenue bonds	(591,519)	(316,882)
Net cash used by capital and related financing activities	(6,035,299)	(7,136,627)
 <b>Cash Flow From Investing Activities</b>		
Purchase of investments	(22,084,694)	(23,578,927)
Maturity of investments	20,606,535	17,050,380
Investment earnings	170,778	114,524
Net cash used by investing activities	(1,307,381)	(6,414,023)
 Increase (decrease) in cash and cash equivalents	1,228,831	(7,321,491)
 Cash and cash equivalents - beginning of year	14,142,696	21,464,187
 Cash and cash equivalents - end of year	\$ 15,371,527	\$ 14,142,696

The notes to the financial statements are an integral part of these statements.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Statements of Cash Flows, Continued**  
**For the Fiscal Years Ended September 30,**

	<b>2017</b>	<b>2016</b>	
<b>Reconciliation of operating income (loss) to net cash provided by operating activities</b>			
Operating income (loss)	\$ 3,175,506	\$ (267,383)	
Adjustments to reconcile operating loss to net cash provided by operating activities:			
Depreciation expense	3,823,252	5,002,225	
Non-operating revenue	716,346	580,544	
Changes in assets and liabilities:			
(Increase) in receivables, net	(128,778)	(94,232)	
Decrease in grant receivable	-	119,238	
Increase in inventory	(3,821)	(32,774)	
(Increase) decrease in prepaid expenses	93,698	(100,657)	
Decrease in net pension assets	-	1,953,444	
Increase (decrease) in pension related deferred outflows	445,275	(1,716,516)	
Decrease in accounts payable	(64,194)	(104,947)	
Decrease in due to primary government	(31,258)	(30,362)	
Increase (decrease) in other liabilities	(86,835)	76,800	
Increase (decrease) in liability for compensated absences	(13,700)	70,561	
Increase in OPEB (retiree health care plan) obligation	297,589	336,971	
Increase in net pension obligation	130,228	193,753	
Increase (decrease) in pension related deferred inflows	(36,586)	(37,516)	
Increase in customer deposits	254,789	280,010	
Net cash provided by operating activities	\$ 8,571,511	\$ 6,229,159	
	<b>2017</b>	<b>2016</b>	<b>Increase (Decrease)</b>
<b>Reconciliation of total cash and cash equivalents:</b>			
Unrestricted cash and cash equivalents	\$ 11,249,565	\$ 9,906,621	\$ 1,342,944
Restricted cash and cash equivalents	4,121,962	4,236,075	(114,113)
Total cash and cash equivalents	\$ 15,371,527	\$ 14,142,696	\$ 1,228,831
<b>Supplemental disclosure of noncash financing activities:</b>			
Water lines, sewer mains and related infrastructure contributed to the System by developers.	\$ 432,882	\$ 219,410	

# **NOTES TO FINANCIAL STATEMENTS**

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Notes to the Financial Statements**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

Reporting Entity

The City of Harlingen Waterworks System (the System) is a component unit of the City of Harlingen, Texas (the City). The System provides water and sewer services to the residents of the City. Activities of the System include administration, operations and maintenance of the water treatment and distribution system and the sewer collection and treatment system, billing and collection activities. The System also accounts for the accumulation of resources for, and the payment of long-term debt principal and interest for water and sewer debt. All costs are financed through charges to utility customers with rates reviewed regularly and adjusted, if necessary, to ensure integrity of the funds.

As provided by the Charter of the City of Harlingen, the City Commission appoints the Utility Board of Trustees. The Board of Trustees functions as the decision and policy making body for all activities related to the System. The City Commission approves rates for user charges, annual budgets, and bond issuance authorizations.

The accompanying financial statements present the financial position, results of operations, and cash flows of the System, and are not intended to present the financial position, results of operations, or cash flows of the City of Harlingen. The financial statements of the System are included in the comprehensive annual financial report of the City of Harlingen as a discretely presented component unit.

Measurement Focus, Basis of Accounting, and Financial Statement Presentation

The System's financial statements are reported using the economic resources measurement focus and the accrual basis of accounting. All assets and liabilities (whether current or non-current) and all deferred outflows and inflows of resources are included in the Statement of Net Position. The operating statements present increases (revenues) and decreases (expenses) in net position. Under the accrual basis of accounting, revenues are recognized when earned, including unbilled water and sewer services which are accrued. Expenses are recorded at the time the liability is incurred, regardless of the timing of related cash flows. The accounting objectives are determination of net income, financial position and cash flow.

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with the fund's principal ongoing operations. The principal operating revenues of the System are charges to customers for sales and services. Operating expenses include the cost of personnel and contractual services, supplies and depreciation on capital assets. Revenues and expenses not meeting these definitions are reported as non-operating revenues and expenses.

The accounting and reporting policies of the System relating to the accompanying financial statements conform to accounting principles generally accepted in the United States of America (GAAP) applicable to state and local governments. Generally accepted accounting principles for local governments include those principles prescribed by the Governmental Accounting Standards Board (GASB).

Cash and Investments

The System's cash and cash equivalents include cash on hand, demand deposits, certificates of deposit, and investments with original maturity dates of three months or less from the date of acquisition.

Investments in government pools are recorded at amortized cost. All other investments are recorded at fair value based upon current market conditions. Fair value is the amount at which a financial instrument could be exchanged in a current transaction between willing parties.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Notes to the Financial Statements**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued**

Receivables and Payables

Accounts receivable represent amounts due from customers for services and user charges, and are presented net of an allowance for uncollectible accounts. The allowance for uncollectible accounts is calculated as a percentage of operating revenue, using the two most recent fiscal years' data.

Outstanding balances between the System and the City of Harlingen are reported as "due to or due from" the primary government. The System performs customer billing and collection services for the City's garbage services. Customer payments collected on behalf of the City are remitted to the City monthly. Amounts collected from garbage customers within the month of September, as well as other reimbursable expenses incurred by the City on behalf of the System, are reflected as "due to the primary government" at fiscal year-end.

Inventories

Inventories are valued at cost using the first-in, first-out (FIFO) method. Inventories are recorded as expenses when used rather than when purchased.

Prepaid Assets

Certain payments made to vendors for goods and services that will benefit future accounting periods are recorded as prepaid items in the financial statements.

Restricted Assets

Certain funds of the System are classified as restricted assets on the statement of net position, because their use is restricted for specific purposes defined and adopted by legislative action. Funds restricted include amounts accumulated for debt service payments over the next twelve months (Debt Service); the proceeds of revenue bond issuances that are restricted for the acquisition or construction of capital assets (Revenue Bond Proceeds); amounts set aside to fund asset replacements (Replacement Reserve); accumulated customer deposits; as well as accumulated capital facilities user impact fees (Impact Fees).

When both restricted and unrestricted resources are available for use, it is the System's policy to use restricted resources first, then unrestricted resources as they are needed.

Capital Assets

Capital assets which include property, plant, equipment, and infrastructure assets are reported in the System's financial statements. All purchased capital assets are valued at historical cost or estimated historical cost if actual historical cost is not available. Donated capital assets are valued at their estimated fair value on the date donated. Capital assets, other than infrastructure assets, are defined by the System as assets with an initial, individual cost of more than \$3,000 and an estimated useful life in excess of three years. Infrastructure assets are reported on a network basis.

Interest incurred during the construction phase of capital assets is included as part of the capitalized value of the assets constructed. The amount of interest capitalized is determined by applying the System's weighted average interest rate to the average cumulative expenditures from inception to completion of the project.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Notes to the Financial Statements, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued**

Capital assets are depreciated using the straight-line method over the following useful lives:

Asset	Years
Buildings and improvements	10-40
Collection lines and lift stations	12-40
Production and treatment facilities	20-40
Furniture and fixtures	5-10
Equipment	3-10
Vehicles	3-7

Compensated Absences

The System's policy allows employees to accumulate earned but unused vacation and sick pay benefits. Upon termination, employees may be paid for accumulated vacation leave up to a maximum of 144 hours. It is the policy of the System to recognize an expense and a liability as the benefits accrue to employees. The accompanying financial statements reflect the vested or accumulated vacation leave accrued through the end of the fiscal year. In accordance with GASB No. 16 "Accounting for Compensated Absences", the System uses the vesting method of calculating the estimated liability for sick leave. The liability recorded by the System includes the maximum allowable benefit for employees who currently are eligible to receive the termination sick pay benefit, as well as an estimate for those employees who are expected to become eligible in the future. At termination of employment, depending upon length of service, employees are eligible to receive 50% of unused sick leave, up to a maximum of 360 hours.

Pensions

For purposes of measuring the net pension liability, pension related deferred outflows and inflows of resources, and pension expense, System specific information about its Fiduciary Net Position in the Texas Municipal Retirement System (TMRS) and additions to/deductions from the System's Fiduciary Net Position have been determined on the same basis as they are reported by TMRS. For this purpose, plan contributions are recognized in the period that compensation is reported for the employee, which is when contributions are legally due. Benefit payments and refunds are recognized when due and payable in accordance with the benefit terms. Investments are reported at fair value. Information regarding the System's Total Pension Liability is obtained from TMRS through a report prepared for the System by TMRS' consulting actuary, Gabriel Roeder Smith & Company, in compliance with GASB Statements No. 68, Accounting and Financial Reporting for Pensions; and No. 71, Pension Transition for Contributions made Subsequent to the Measurement Date.

Deferred Outflows/Inflows of Resources

In addition to assets, the statement of financial position reports a separate section for deferred outflows of resources. This separate financial statement element represents a consumption of net position that applies to a future period(s) and so will not be recognized as an outflow of resources (expense) until then. The System has the following items that qualify for reporting in this category.

- Deferred charges on refunding - A deferred charge on refunding results from the difference between the carrying value of refunded debt and its reacquisition price. This amount is deferred and amortized over the shorter of the life of the refunded or refunding debt.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Notes to the Financial Statements, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued**

- Pension contributions after measurement date - These contributions are deferred and recognized in the following fiscal year.
- Difference in projected and actual earnings on pension assets - This difference is deferred and amortized over a closed five year period.
- Changes in actuarial assumptions used to determine pension liability - This difference is deferred and amortized over the estimated average remaining lives of all members, determined as of the measurement date.

In addition to liabilities, the statement of financial position reports a separate section for deferred inflows of resources. This separate financial statement element represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. The System has two types of items that qualify for reporting in this category. The difference in expected and actual pension experience is deferred and recognized over the estimated average remaining lives of all members, determined as of the measurement date; and the difference in projected and actual earnings on pension assets is deferred and recognized over a closed five year period.

Net Position

Net position represents the difference between assets and deferred outflows of resources less liabilities and deferred inflows of resources. Net investment in capital assets consists of capital assets net of accumulated depreciation, reduced by the outstanding balances of borrowing spent for the acquisition, construction or improvement of those assets. Net position is reported as restricted when there are limitations imposed on their use either through enabling legislation adopted by the System and or the City, or through external restrictions imposed by creditors, grantors or laws or regulations of other governments.

Budgetary Control

A formal budgetary process is employed by the System as a management control device.

The System's fiscal year is the twelve-month period beginning October 1. Department managers submit to the General Manager a budget of estimated expenses for the ensuing fiscal year. The General Manager subsequently submits a budget of estimated expenses and revenues to the Utility Board of Trustees. After approval by the Utility Board of Trustees, the budget is forwarded to the City Commission. The budget is legally enacted through passage of an ordinance.

The General Manager is authorized to transfer budgeted amounts between line items and departments. Any revisions that alter total expenses must be approved by the Utility Board of Trustees.

Budgeted amounts are as originally adopted, or as amended by the Utility Board of Trustees. Individual amendments were not material in relation to the original appropriations, which were adopted.

The Schedule of Revenues, Expenses and Changes in Net Position, Comparison of Actual to Budget, included as other supplementary information in this report, presents a comparison of budgetary data to actual results.

Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Actual results could differ from those estimates.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Notes to the Financial Statements, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES – Continued**

Comparative Data/Reclassifications

Comparative data for the prior year have been presented in the financial statements in order to provide an understanding of the changes in the financial position and operations of the fund. Certain amounts presented in the prior year's financial statements have been reclassified to conform to the current year's presentation.

**2. DEPOSITS AND INVESTMENTS**

System Policies and Legal Contractual Provisions Governing Deposits

State statutes govern the deposit and investment of all funds of the System. Texas Local Government Code, Chapter 105. "Depositories for Municipal Funds" dictates the selection of and requirements for financial institutions to serve as depositories for public funds. Texas Government Code, Chapter 2257, "Collateral for Public Funds" governs security for a deposit of public funds.

The System's deposits, including certificates of deposit, at September 30, 2017 and during the year were fully insured by FDIC insurance or were collateralized by securities pledged to the System and held by the System's agent bank in the System's name, or were secured by Irrevocable standby letters of credit.

At September 30, 2017, the carrying amount of the System's deposits was as follows:

	2017		
	BBVA Compass	Southside Bank	Green Bank
	Demand Deposit	Money Market	Money Market
Book Value	\$ 5,286,204	\$ 2,561,846	\$ 1,012,643
Bank Balance	5,702,283	2,561,846	1,012,643
FDIC Coverage	250,000	250,000	250,000
Collateral	13,250,000	2,492,530	2,822,000

At September 30, 2016, the carrying amount of the System's deposits was as follows:

	2016		
	BBVA Compass	Southside Bank	Green Bank
	Demand Deposit	Money Market	Money Market
Book Value	\$ 4,343,143	\$ 2,030,397	\$ 1,003,577
Bank Balance	5,396,972	2,030,397	1,003,577
FDIC Coverage	250,000	250,000	250,000
Collateral	7,650,000	2,717,927	775,000

In addition, the following is disclosed regarding coverage of combined balances on the date of highest deposit:

- a. Primary Depository: BBVA Compass Bank
- b. The highest combined balances of cash on deposit amounted to \$7,048,800 and occurred in the month of July, 2017.
- c. The amount of FDIC coverage as of the date of the highest combined balance on deposit was \$250,000.
- d. An Irrevocable Standby Letter Of Credit in the amount of \$13,250,000 was in force to secure the System's deposits as of the date of the highest combined balance.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Notes to the Financial Statements, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**2. DEPOSITS AND INVESTMENTS (Continued)**

Custodial Credit Risk for Deposits – State law requires governmental entities to contract with financial institutions in which funds will be deposited to secure funds on deposit at the end of each business day. The pledged securities must have a market value of not less than the amount of the deposits, be in the name of the governmental entity and be held by the entity or its agent. The pledge of approved securities is waived only to the extent of the depository bank's dollar amount of Federal Deposit Insurance Corporation ("FDIC") insurance. At September 30, 2017, all System deposits were insured or adequately collateralized.

Foreign Currency Risk for Deposits – Transactions of the System are limited to those backed by domestic currency. The System is not directly exposed to foreign currency risk.

System Policies and Legal Contractual Provisions Governing Investments

The System's investment program is governed by the Public Funds Investment Act (Texas Government Code Chapter 2256), and by the System's investment policy which amplifies the State statutes and prescribes how the System will operate its investment program in accordance with applicable laws and regulations. The Public Funds Investment Act (the "PFIA") contains specific provisions governing investment practices, management responsibilities, the establishment of appropriate policies, and reporting requirements. The investment policy addresses the following areas: suitability; preservation and safety of principal; liquidity; marketability; diversification; allowable investments; acceptable risk levels; expected rates of return; maximum allowable stated maturity; maximum average dollar-weighted maturity allowed; investment staff quality, capabilities and responsibilities; and bid solicitation preferences.

The System's investment policy authorizes the System to invest in the following:

1. Obligations of the United States of America, its agencies and instrumentalities;
2. Direct obligations of the State of Texas or its agencies and instrumentalities;
3. Other obligations, the principal of and interest of which are unconditionally guaranteed or insured by, or backed by the full faith and credit of, the State of Texas or United States of America or their respective agencies and instrumentalities;
4. Obligations of states, agencies thereof, counties, cities, and other political subdivisions of any state having been rated as to investment quality by a nationally recognized investment rating firm, and having received a rating of not less than "A" or its equivalent;
5. Certificates of Deposit and other evidences of deposit at a financial institution that (a) has its main office or a branch office in Texas and is guaranteed or insured by the Federal Deposit Insurance Corporation or its successor or the National Credit Union Share Insurance Fund or its successor; (b) secured by obligations described in 1 through 4 above, that have a market value of not less than the principal amount of the certificates, or (c) secured in any other manner and amount provided by law for deposits of the System, or (d) executed through a depository institution that has its main office or a branch office in Texas and meets the requirements of the Act;
6. Local government investment pools of political subdivisions in the State of Texas, which invest in instruments and follow practices allowed by current law; maintain as an investment objective a \$1.00 net asset value; provide offering circulars containing information required by the Act; provide investment transaction confirmations; provide a monthly report containing information required by the Act; have an advisory board as specified by the Act; are continuously rated no lower than AAA or AAA-m or an equivalent rating by at least one nationally recognized rating service; and are fully compliant with the Act. Participation in an investment pool must be authorized by Resolution of the Utility Board of Trustees;

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Notes to the Financial Statements, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**2. DEPOSITS AND INVESTMENTS (Continued)**

7. No-load government money market mutual funds organized and in compliance with current law; that maintain as an investment objective a \$1.00 net asset value for each share; are registered with and regulated by the Securities and Exchange Commission; are continuously rated no lower than AAA or AAA-m or an equivalent rating by at least one nationally recognized rating service; and have provided to the System a prospectus and other information required by the Securities Exchange Act of 1937 or the Investment Company Act of 1940;
8. Repurchase agreements with a defined termination date, fully collateralized by cash or securities described in 1 above, held in the name of the System by an independent third party custodian contracted by the System, placed through primary government securities dealers or financial institutions doing business in Texas; who have executed a Repurchase Agreement that has been approved by the Utility Board of Trustees of the System.

The PFIA also requires the System to have independent auditors perform test procedures related to investment practices. The System's management believes the System has complied with the requirements of the PFIA and the System's investment policies.

At September 30, 2017, the carrying value of the System's portfolio was as follows:

<u>Investment Type</u>	<u>Carrying Value</u>	<u>Percentage of Total</u>	<u>Weighted Average Life</u>	<u>Credit Risk</u>
Certificates of Deposit				
BBVA Compass	\$ 6,000,000	27.87%	23	-
Legacy Bank	7,019,294	32.60%	67	-
Green Bank	2,000,000	9.29%	50	-
Public Fund Pools				
TexSTAR	3,225,926	14.98%	1	AAAm
TexPool	3,284,908	15.26%	1	AAAm
Total	<u>\$ 21,530,128</u>	<u>100.00%</u>		

At September 30, 2016, the carrying value of the System's portfolio was as follows:

<u>Investment Type</u>	<u>Carrying Value</u>	<u>Percentage of Total</u>	<u>Weighted Average Life</u>	<u>Credit Risk</u>
Certificates of Deposit				
Southside Bank	3,014,648	14.84%	19	-
Legacy Bank	10,526,487	51.84%	103	-
Public Fund Pools				
TexSTAR	3,393,333	16.71%	1	AAAm
TexPool	3,372,246	16.61%	1	AAAm
Total	<u>\$ 20,306,714</u>	<u>100.00%</u>		

The System categorizes its fair value measurements within the fair value hierarchy established by generally accepted accounting principles. The hierarchy is based on the valuation inputs used to measure the fair value of the asset. Level 1 inputs are quoted prices in active markets for identical assets; Level 2 inputs are significant other observable inputs; Level 3 inputs are significant unobservable inputs.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Notes to the Financial Statements, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**2. DEPOSITS AND INVESTMENTS (Continued)**

As of September 30, 2017, the System has certificates of deposit totaling \$15,019,293 valued at cost. The system's investments in government pools at September 30, 2017 totaling \$6,510,834 are recorded at amortized cost.

Public funds investment pools in Texas ("Pools") are established under the authority of the Inter-local Cooperation Act Chapter 79 of the Texas Government Code and are subject to the provisions of the Public Funds Investment Act (the "PFIA"), Chapter 2256 of the Texas Government Code. In addition to other provisions of the PFIA designed to promote liquidity and safety of principal, the PFIA requires Pools to: have an advisory board composed of participants in the pool and other persons who do not have a business relationship with the pool and are qualified to advise the pool; maintain a continuous rating of no lower than AAA or AAAM or an equivalent rating by at least one nationally recognized rating service; and maintain the market value of its underlying investment portfolio within one half of one percent of the value of its shares.

Additional policies and contractual provisions governing deposits and investments for the System are specified below:

**Credit Risk** – In accordance with State law and the System's investment policy, investments in investment pools must be rated no lower than AAA or AAA-m or have an equivalent rating, obligations of states, agencies, counties, and cities must be rated at least A or its equivalent. As of September 30, 2017, the System's investments in TexPool and TexSTAR were rated AAAM by Standard and Poor's.

**Custodial Risk for Investments** – Is the risk that, in the event of the failure of the counter party, the System will not be able to recover the value of its investments or collateral securities that are in the possession of an outside party. The investment pools are not managed by the System and the System does not possess securities that exist in either physical or book entry form.

**Concentration of Credit Risk** – The underlying securities of the investment pools is diversified in terms of investment instruments and maturity scheduling to reduce the risk of loss resulting from over concentration of assets in specific class of investments, specific maturity or specific issuer.

**Interest Rate Risk** – The System's objective is to obtain a reasonable rate of return throughout budgetary and economic cycles, taking into account the investment risk limitations and the cash flow characteristics of the portfolio. Investment maturities are structured to provide cash flow based on anticipated operating needs. At no time, are debt service fund investment maturities allowed to exceed the anticipated cash flow requirements. Market conditions influence the decision to fully extend maturities to the next "unfunded" payment date or to invest in shorter term instruments. Customer deposit funds require the liquidity adequate to cover the return of customer security deposits. Short term-investment pools and money market mutual funds may be utilized as a competitive yield alternative to fixed maturity investments.

**Foreign Currency Risk for Investments** – By virtue of the System's investment policy and the PFIA, the System is not directly exposed to foreign currency risk. The System is not authorized to maintain deposits or investments denominated in a foreign currency.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Notes to the Financial Statements, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**3. ACCOUNTS RECEIVABLE**

Accounts receivable as of September 30 consist of the following:

<u>Description</u>	<u>2017</u>	<u>2016</u>
Water Accounts	\$ 364,403	\$ 329,966
Wastewater Accounts	398,321	408,989
Customer invoices and charges	194,283	206,769
Other	31,642	58,147
Total invoiced accounts receivable	988,649	1,003,871
Unbilled customer charges:		
Water	705,000	638,000
Wastewater	752,000	683,000
Total unbilled customer charges	1,457,000	1,321,000
Total accounts receivable	2,445,649	2,324,871
Less allowance for uncollectible accounts	(204,000)	(212,000)
Total Accounts receivable (net)	\$ 2,241,649	\$ 2,112,871

**4. RESTRICTED ASSETS**

Restricted assets as of September 30 consist of the following:

<u>Cash and cash equivalents</u>	<u>2017</u>	<u>2016</u>
Customer deposits	\$ 282,602	\$ 527,813
Impact fees - replacement reserve	1,396,649	621,765
Front footage and tie in fees - replacement reserve	489,824	485,439
Debt service fund	1,684,481	1,675,851
Series 2015A bond proceeds	268,406	925,207
<u>Investments</u>		
Customer deposits	2,125,000	1,625,000
Series 2015A bond proceeds	3,505,467	6,019,727
	\$ 9,752,429	\$ 11,880,802

The ordinances authorizing the issuance of the Waterworks and Sewer System Revenue Bonds require the establishment of an interest and sinking fund. The interest and sinking fund is used to pay the principal of and interest on the bonds, as such comes due. Deposits are made into the interest and sinking fund in equal monthly installments sufficient to pay the next interest payment due and the next maturing principal of the bonds. Those same ordinances restrict the use of revenue bond proceeds for the purpose of improving, enlarging, or equipping the water and wastewater systems.

Capital facilities user impact fees and front footage and tie-in fees were established as restricted assets by ordinance of the City of Harlingen. Customer security deposits are held for the benefit of the System's customers to satisfy utility account balances upon termination of service.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Notes to the Financial Statements, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**5. CAPITAL ASSETS**

During the fiscal year, it was determined the estimated service life of a number of infrastructure assets was too conservative. To more accurately depreciate the remaining value of the assets, the useful life was extended to a more realistic number. Extending the estimated useful life of the assets reduced the annual depreciation expense in the year ended September 30, 2017 by approximately \$1,250,000.

Interest incurred during the construction phase of capital assets and included as part of the capitalized value of the assets constructed in the fiscal years ended September 30 2017 and 2016, respectively was \$199,712 and \$255,316.

Capital asset activity for the System for the year ended September 30, 2017 was as follows:

	Balance <u>9/30/2016</u>	Reclass & <u>Additions</u>	Reclass & <u>Disposals</u>	Balance <u>9/30/2017</u>
Capital assets not being depreciated				
Water rights	\$ 5,423,369	\$ -	\$ -	\$ 5,423,369
Land & land rights	1,202,089	6,864	-	1,208,953
Construction in progress	<u>10,692,042</u>	<u>3,887,284</u>	<u>(11,369,636)</u>	<u>3,209,690</u>
Total capital assets not being depreciated	<u>17,317,500</u>	<u>3,894,148</u>	<u>(11,369,636)</u>	<u>9,842,012</u>
Other capital assets				
Vehicles	2,972,049	217,407	-	3,189,456
Water production plant	27,630,188	22,755	-	27,652,943
Water transmission facilities and equipment	55,166,665	344,113	(38,400)	55,472,378
Wastewater treatment plant	23,325,702	9,513,147	(1,452,342)	31,386,507
Wastewater collection lines, lift stations and equipment	50,597,244	2,127,187	(42,772)	52,681,659
Laboratory building and equipment	315,638	100,326	-	415,964
Pretreatment buildings and equipment	76,801	-	-	76,801
Office buildings and equipment	<u>3,980,129</u>	<u>101,135</u>	<u>(24,760)</u>	<u>4,056,504</u>
Total capital assets being depreciated	<u>164,064,416</u>	<u>12,426,070</u>	<u>(1,558,274)</u>	<u>174,932,212</u>
Less accumulated depreciation				
Vehicles	(2,132,568)	(92,822)	-	(2,225,390)
Water production plant	(20,059,552)	(601,822)	-	(20,661,374)
Water transmission facilities and equipment	(34,572,037)	(845,569)	-	(35,417,606)
Wastewater treatment plant	(21,094,782)	(1,022,687)	1,227,646	(20,889,823)
Wastewater collection lines, lift stations and equipment	(30,420,046)	(1,067,830)	28,516	(31,459,360)
Laboratory building and equipment	(230,418)	(23,911)	-	(254,329)
Pretreatment buildings and equipment	(74,043)	(1,084)	-	(75,127)
Office buildings and equipment	<u>(2,986,606)</u>	<u>(167,528)</u>	<u>24,760</u>	<u>(3,129,374)</u>
Total accumulated depreciation	<u>(111,570,052)</u>	<u>(3,823,252)</u>	<u>1,280,922</u>	<u>(114,112,382)</u>
Capital assets, net of accumulated depreciation	<u>\$ 69,811,864</u>	<u>\$ 12,496,966</u>	<u>\$ (11,646,988)</u>	<u>\$ 70,661,842</u>

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Notes to the Financial Statements, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**5. CAPITAL ASSETS (Continued)**

Capital asset activity for the System for the year ended September 30, 2016 was as follows:

	Balance 9/30/2015	Reclass & Additions	Reclass & Disposals	Balance 9/30/2016
Capital assets not being depreciated				
Water rights	\$ 5,423,369	\$ -	\$ -	\$ 5,423,369
Land & land rights	1,189,507	12,582	-	1,202,089
Construction in progress	4,997,226	6,380,135	(685,319)	10,692,042
Total capital assets not being depreciated	<u>11,610,102</u>	<u>6,392,717</u>	<u>(685,319)</u>	<u>17,317,500</u>
Other capital assets				
Vehicles	2,834,751	215,193	(77,895)	2,972,049
Water production plant	27,649,069	-	(18,881)	27,630,188
Water transmission facilities and equipment	54,193,453	1,014,194	(40,982)	55,166,665
Wastewater treatment plant	23,153,390	180,712	(8,400)	23,325,702
Wastewater collection line, lift stations and equipment	50,442,241	155,003	-	50,597,244
Laboratory building and equipment	296,167	19,471	-	315,638
Pretreatment buildings and equipment	76,801	-	-	76,801
Office buildings and equipment	3,953,002	27,127	-	3,980,129
Total capital assets being depreciated	<u>162,598,874</u>	<u>1,611,700</u>	<u>(146,158)</u>	<u>164,064,416</u>
Less accumulated depreciation				
Vehicles	(1,945,720)	(264,744)	77,896	(2,132,568)
Water production plant	(19,433,319)	(644,809)	18,576	(20,059,552)
Water transmission facilities and equipment	(33,151,056)	(1,423,565)	2,584	(34,572,037)
Wastewater treatment plant	(20,318,564)	(781,967)	5,749	(21,094,782)
Wastewater collection line, lift stations and equipment	(28,711,894)	(1,708,152)	-	(30,420,046)
Laboratory building and equipment	(211,097)	(19,321)	-	(230,418)
Pretreatment buildings and equipment	(72,956)	(1,087)	-	(74,043)
Office buildings and equipment	(2,828,026)	(158,580)	-	(2,986,606)
Total accumulated depreciation	<u>(106,672,632)</u>	<u>(5,002,225)</u>	<u>104,805</u>	<u>(111,570,052)</u>
Capital assets, net of accumulated depreciation	<u>\$ 67,536,344</u>	<u>\$ 3,002,192</u>	<u>\$ (726,672)</u>	<u>\$ 69,811,864</u>

**6. DUE TO PRIMARY GOVERNMENT**

At September 30, 2017 and 2016 the System was liable to the City of Harlingen for amounts collected by the System from customers utilizing City garbage collection services; and amounts the City billed to the System for insurance premiums, and for other services provided by the City on behalf of the System in the amounts of \$111,801 and \$143,059 respectively.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Notes to the Financial Statements, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**7. PAYABLE FROM RESTRICTED ASSETS**

Payable from restricted assets as of September 30 consists of the following:

	<u>2017</u>	<u>2016</u>
Current:		
Accrued interest	\$ 322,180	\$ 334,305
Customer deposits	300,000	267,813
Noncurrent:		
Customer deposits	2,107,602	1,885,000
Total	\$ 2,729,782	\$ 2,487,118

**8. LONG-TERM DEBT**

Revenue Bonds are used to finance the acquisition and construction of major capital improvements for the water and sewer system and related facilities. The revenue bonds are special obligations of the System solely secured by a first lien on and pledge of the net revenues of the combined waterworks and sewer system. Net revenues are defined in the respective covenants and are more fully explained therein as the gross revenues of the System less the expenses of operation and maintenance of the System. Depreciation and payments into and out of the required interest and sinking and the reserve funds are not considered expenses of operation and maintenance. Remaining revenues may then be used for any lawful purpose.

In October 2010, the System issued the Waterworks and Sewer System Revenue Bonds, Series 2010A in the principal amount of \$6,500,000 to provide funding for the System's ongoing capital improvement program and to cover the cost of issuance. Simultaneously, in order to achieve a debt service savings due to favorable interest rates. The Waterworks and Sewer System Revenue Refunding Bonds, Series 2010B were issued, in the principal amount of \$4,205,000. The proceeds from the sale of the Series 2010B Bonds were used for purpose of paying costs of issuance and refunding all of the then outstanding Waterworks and Sewer System Revenue Bonds, Series 2000 in the amount of \$1,220,000 and Series 2003 in the amount of \$4,410,000.

The Series 2010B Bond proceeds, along with other available funds of the System, were deposited with an escrow agent and irrevocably pledged to the payment of principal and interest on the refunded Bonds until the respective call dates. As a result, the refunded obligations are considered defeased, and the liability for those bonds has been removed from the System's financial statements. As of September 30, 2017, all Series 2000 and Series 2003 Bonds have been retired.

In September 2015, the System issued the Waterworks and Sewer System Revenue Bonds, Series 2015A in the principal amount of \$12,000,000 to provide funding for the System's ongoing capital improvement program and to cover the cost of issuance. Simultaneously, in order to achieve a debt service savings due to favorable interest rates, the Waterworks and Sewer System Revenue Refunding Bonds, Series 2015B were issued, in the principal amount of \$6,475,000. The proceeds from the sale of the Series 2015B Bonds were used for the purpose of refunding all of the then outstanding Waterworks and Sewer System Revenue Refunding Bonds, Series 2005 in the amount of \$2,620,000; and the Waterworks and Sewer System Revenue Bonds, Series 2005A in the amount of \$4,435,000 and to pay the costs of issuance.

The Series 2015B Bond proceeds, along with other available funds of the System, were deposited with an escrow agent for payment of principal and interest on the refunded debt until the respective call dates of November 1, 2015 through November 1, 2019. As a result, the refunded obligations are considered defeased, and the liability for those bonds has been removed from the System's financial statements. As of September 30, 2017, Series 2005A Bonds in the principal amount of \$765,000 with maturities of November 1, 2017 through November 1, 2019 have not been redeemed.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Notes to the Financial Statements, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**8. LONG-TERM DEBT (Continued)**

The bonds carry interest rates as set out below with the interest payment dates of May 1<sup>st</sup> and November 1<sup>st</sup>; and principal payments due annually on November 1<sup>st</sup>. The bond ordinances authorizing these issues require establishing an interest and sinking fund; and, if certain financial ratios are not met, a reserve fund. A Credit Facility may be used as a substitute for or to replace cash or investments in the reserve fund. In addition, a provision in the ordinances requires that rates for service be adjusted if certain financial ratios are not met. Management of the System believes it is in compliance with all significant financial requirements of the bond ordinances as of September 30, 2017.

As of September 30, 2017, revenue bonds outstanding are as follows:

<u>Bond Issue</u>	<u>Original Amount</u>	<u>Interest Rates</u>	<u>Issue Date</u>	<u>Maturity Date</u>	<u>Principal Outstanding</u>
Waterworks and Sewer System Revenue, Series 2010A	\$ 6,500,000	2.0-4.00%	9/15/2010	11/1/2035	\$ 5,865,000
Waterworks and Sewer System Revenue Refunding, Series 2010B	\$ 4,205,000	2.0-3.00%	9/15/2010	11/1/2020	\$ 475,000
Waterworks and Sewer System Revenue, Series 2015A	\$ 12,000,000	2.0-3.75%	9/1/2015	11/1/2035	\$ 11,550,000
Waterworks and Sewer System Revenue Refunding, Series 2015B	\$ 6,475,000	2.0-3.25%	9/1/2015	11/1/2035	<u>\$ 5,795,000</u>
					<u>\$ 23,685,000</u>

Annual debt service requirements to maturity for revenue bonds are as follows:

<u>Year ending September 30,</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2018	\$ 1,480,000	\$ 757,606	\$ 2,237,606
2019	1,525,000	719,107	2,244,107
2020	1,565,000	672,756	2,237,756
2021	1,615,000	625,056	2,240,056
2022	1,015,000	585,444	1,600,444
2023-2027	5,565,000	2,419,288	7,984,288
2028-2032	6,250,000	1,430,009	7,680,009
2033-2036	4,670,000	370,819	5,040,819
Total	<u>\$ 23,685,000</u>	<u>\$ 7,580,085</u>	<u>\$ 31,265,085</u>

**9. CHANGES IN LONG TERM LIABILITIES**

Long-term liability activity for the year ended September 30, 2017, was as follows:

	<u>Balance October 1</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance September 30</u>	<u>Due within one year</u>
Bonds payable	\$ 25,140,000	\$ -	\$(1,455,000)	\$ 23,685,000	\$ 1,480,000
Deferred amounts for discounts and premiums	201,003	-	(29,834)	171,169	27,230
Total bonds payable	25,341,003	-	(1,484,834)	23,856,169	1,507,230
Compensated absences	776,517	567,928	(581,628)	762,817	572,000
Retiree health care obligations	3,542,478	631,733	(334,144)	3,840,067	-
Net pension obligation	193,753	680,909	(550,681)	323,981	-
Customer Deposits	2,152,813	545,704	(290,915)	2,407,602	300,000
Total	<u>\$ 32,006,564</u>	<u>\$ 2,426,274</u>	<u>\$ (3,242,202)</u>	<u>\$ 31,190,636</u>	<u>\$ 2,379,230</u>

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Notes to the Financial Statements, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**9. CHANGES IN LONG TERM LIABILITIES (Continued)**

Long-term liability activity for the year ended September 30, 2016, was as follows:

	Balance <u>October 1</u>	<u>Additions</u>	<u>Reductions</u>	Balance <u>September 30</u>	Due within <u>one year</u>
Bonds payable	\$ 25,460,000	\$ -	\$ (320,000)	\$ 25,140,000	\$ 1,455,000
Deferred amounts for discounts and premiums	233,261	-	(32,258)	201,003	29,834
Total bonds payable	25,693,261	-	(352,258)	25,341,003	1,484,834
Compensated absences	705,956	564,851	(494,290)	776,517	543,517
Retiree health care obligations	3,205,507	678,313	(341,342)	3,542,478	-
Net pension obligation (asset)	(1,953,444)	2,639,174	(491,977)	193,753	-
Customer Deposits	1,872,803	513,000	(232,990)	2,152,813	267,813
Total	<u>\$ 29,524,083</u>	<u>\$ 4,395,338</u>	<u>\$ (1,912,857)</u>	<u>\$ 32,006,564</u>	<u>\$ 2,296,164</u>

**10. COMMITMENTS AND CONTINGENT LIABILITIES**

The System is currently under contract with five wholesale customers (users) to provide treated water. These agreements provide for the treatment of an aggregate minimum of at least 250,000,000 gallons annually. The contracts have various expiration dates ranging from year 2016 to 2054. The System has contracted to provide wastewater treatment services to two wholesale customers. The combined annual flow is estimated to be 250,000,000 gallons.

As of September 30, 2017, the System had open purchase orders for construction projects, operating supplies and equipment in the amount of \$2,272,511. The projects include water treatment, transmission and distribution system improvements and wastewater treatment and collection system improvements. These commitments will be funded with bond proceeds, and unrestricted cash.

Amounts received or receivable from grant agencies are subject to audit and adjustment by the grantors or their representatives. Any liability for reimbursement which may arise as the result of these audits is not believed to be material.

Various claims are pending against the System. In the opinion of System management, after consultation with legal counsel, the potential loss on all claims will not materially affect the System's financial position, results of operations, or cash flows.

**11. RISK MANAGEMENT**

The System is exposed to various uncertainties for losses related to intentional and unintentional torts; theft of, damage to and destruction of real and personal property; errors and omissions; catastrophes, medical and dental claims by employees; employee illnesses and injuries and pollution claims for which the Waterworks carries commercial insurance coverage. There have been no significant reductions in insurance coverage from the previous year. No negotiated settlements or jury awards have exceeded policy limits in any of the past three years. The Waterworks is a member of an intergovernmental risk pool. The risk pool is an inter-local non-assessable agency with present unreserved resources in excess of \$344,532,000 (as of September 30, 2017, the most recently audited financial statements completed for the risk pool). Reinsurance is provided by several A and A++ rated companies in amounts ranging from \$10,000,000 to \$100,000,000 depending on the type of insurance coverage. The Waterworks must promptly pay contributions to the risk pool as outlined by the coverage contracts, comply with underwriting standards and implement loss control recommendations deemed necessary by a risk pool representative due to an eminent high risk of loss situation. City and System management are not aware of any pending or alleged claims that could exceed the policy limits of the present insurance coverage.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Notes to the Financial Statements, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**12. NET POSITION**

Net position is composed of three categories: Invested in capital assets net of related debt, restricted net position, and unrestricted net position. The following schedule provides detail of the categories of net position as of September 30:

	<u>2017</u>	<u>2016</u>
Net investment in capital assets		
Net capital assets	\$ 70,661,842	\$ 69,811,864
Revenue bonds payable (net of unspent Series 2015A bond proceeds)	<u>(20,082,296)</u>	<u>(18,396,069)</u>
Net investment in capital assets	<u>50,579,546</u>	<u>51,415,795</u>
 Net position restricted for:		
Debt service:		
Cash, cash equivalents and investments	1,684,481	1,675,851
Accrued interest payable	(322,180)	(334,305)
System expansion (Impact fees):		
Cash, cash equivalents and investments	1,396,648	621,765
System expansion (Front footage & tie-in fees)		
Cash, cash equivalents and investments	489,824	485,439
Capital Improvements (Bond proceeds):		
Cash, cash equivalents and investments	3,773,873	6,944,934
Customer deposits:		
Cash, cash equivalents and investments	2,407,602	2,152,813
Payable to utility customers	(2,407,602)	(2,152,813)
Employee pensions:		
Deferred outflows related to pensions	1,543,195	1,988,470
Net Pension Obligations	(323,981)	(193,753)
Deferred inflows related to pensions	<u>(56,456)</u>	<u>(93,042)</u>
Restricted net position	<u>8,185,404</u>	<u>11,095,359</u>
Unrestricted net position	<u>14,324,992</u>	<u>6,143,057</u>
Total net position	<u>\$ 73,089,942</u>	<u>\$ 68,654,211</u>

**13. MAJOR CUSTOMERS**

For the years ended September 30, 2017 and 2016, no single customer provided more than 10% of water revenues or wastewater revenues. For the years ended 2017 and 2016, the top ten wastewater customers provided approximately \$1,478,329 and \$1,459,351 or 13.60% and 14.47% of wastewater sales revenues. The top ten water customers generated approximately \$1,332,814 and \$1,182,936 or 12.55% and 12.66% of the water sales revenues, for September 30, 2017 and 2016, respectively.

**14. DEFINED BENEFIT PENSION PLAN**

Plan Description

The System participates as one of 872 plans in the nontraditional, joint contributory, hybrid defined benefit pension plan administered by the Texas Municipal Retirement System (TMRS). TMRS is an agency created by the State of Texas and administered in accordance with the TMRS Act, Subtitle G, Title 8, Texas Government Code (the TMRS Act) as an agent multiple-employer retirement system for municipal employees in the State of Texas.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Notes to the Financial Statements, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**14. DEFINED BENEFIT PENSION PLAN (Continued)**

The TMRS Act places the general administration and management of the TMRS System with a six-member Board of Trustees. Although the Governor, with the advice and consent of the Senate, appoints the Board, TMRS is not fiscally dependent on the State of Texas. TMRS's defined benefit pension plan is a tax-qualified plan under Section 401(a) of the Internal Revenue Code. TMRS issues a publicly available comprehensive annual financial report (CAFR) that can be obtained at [www.tmr.com](http://www.tmr.com).

All eligible employees of the System are required to participate in TMRS.

Benefits Provided

TMRS provides retirement, disability, and death benefits. Benefit provisions are adopted by the governing body of the Harlingen Waterworks System, within the options available in the state statutes governing TMRS.

At retirement, the benefit is calculated as if the sum of the employee's contributions, with interest, and the System-financed monetary credits, with interest, were used to purchase an annuity. Members may choose to receive their retirement benefit in one of seven actuarially equivalent payment options. Members may also choose to receive a portion of their benefit as a Partial Lump Sum Distribution in an amount equal to 12, 24, or 36 monthly payments, which cannot exceed 75% of the member's deposits and interest.

Plan provisions for the System were as follows:

Employee deposit rate	7%
Matching ration (System to employee)	1 to 1
Years required for vesting	5
Service retirement eligibility	20 yrs at any age; 5 yrs at age 60 and above
Updated service credit	0%
Annuity increase (to retirees)	0% of CPI
Supplemental death benefit	Active Employees & Retirees

At the December 31 valuation and measurement date, the following employees were covered by the benefit terms:

	2016	2015
Retirees or beneficiaries currently receiving benefits	111	105
Inactive employees entitled to but not yet receiving benefits	45	46
Active employees	141	142
Total	297	293

Contributions

Under the state law governing TMRS, the contribution rate for each participant is determined annually by the consulting actuary, using the Entry Age Normal (EAN) actuarial cost method. The actuarially determined rate is the estimated amount necessary to finance the cost of benefits earned by employees during the year, with an additional amount to finance any unfunded accrued liability.

Employees for the Harlingen Waterworks System were required to contribute 7% of their annual gross earnings during the fiscal year. The contribution rates for the System were 1.08%, 0.59%, and 1.75% in calendar years 2015, 2016, and 2017 respectively. The System's contributions to TMRS for the fiscal years ended September 30, 2015, 2016, and 2017 were \$75,455, \$43,964, \$89,045, respectively, and were equal to the required contributions.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Notes to the Financial Statements, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**14. DEFINED BENEFIT PENSION PLAN (Continued)**

Net Pension Liability

The System's Net Pension Liability (NPL) was measured as of December 31, 2016. The Total Pension Liability (TPL) used to calculate the Net Pension Liability was determined by an actuarial valuation as of that date.

Actuarial Assumptions:

The Total Pension Liability in the December 31, 2016 actuarial valuation was determined using the following actuarial assumptions:

Inflation	2.5% per year
Overall payroll growth	3.0% per year
Investment Rate of Return	6.75%, net of pension plan investment expense, including inflation

Salary increases were based on a service-related table. Mortality rates for active members, retirees, and beneficiaries were based on the gender-distinct RP2000 Combined Healthy Mortality Table, with Blue Collar Adjustment, with male rates multiplied by 109% and female rates multiplied by 103%. The rates are projected on a fully generational basis by scale BB to account for future mortality improvements. For disabled annuitants, the gender-distinct RP2000 Combined Healthy Mortality Tables with Blue Collar Adjustment are used, with male rates multiplied by 109% and female rates multiplied by 103% with a 3-year set-forward for both males and females. In addition, a 3% minimum mortality rate is applied to reflect the impairment for younger members who become disabled. The rates are projected on a fully generational basis by scale BB to account for future mortality improvements subject to the 3% floor.

Actuarial assumptions used in the December 31, 2016 valuation were based on the results of actuarial experience studies. This experience study was for the period December 31, 2010 through December 31, 2014. Healthy post-retirement mortality rates and annuity purchase rates were updated based on a Mortality Experience Investigation Study covering 2009 through 2011, and dated December 31, 2013. These assumptions were first used in the December 31, 2013 valuation, along with a change to the Entry Age Normal (EAN) actuarial cost method. Assumptions are reviewed annually. No additional changes were made for the 2015 valuation. After the Asset Allocation Study analysis and experience investigation study, the Board amended the long-term expected rate of return on pension plan investments from 7% to 6.75% effective January 1, 2016. Plan assets are managed on a total return basis with an emphasis on both capital appreciation as well as the production of income, in order to satisfy the short-term and long-term funding needs of TMRS.

The pension plan's policy in regard to the allocation of invested assets is established and may be amended by the TMRS Board of Trustees. The long-term expected rate of return on pension plan investments was determined using a building-block method in which best estimate ranges of expected future real rates of return (expected returns, net of pension plan investment expense and inflation) are developed for each major asset class. These ranges are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentage and by adding expected inflation. In determining their best estimate of a recommended investment return assumption under the various alternative asset allocation portfolios, the actuary focused on the area between (1) arithmetic mean (aggressive) without an adjustment for time (conservative) and (2) the geometric mean (conservative) with an adjustment for time (aggressive). At its meeting on July 30, 2015, the TMRS Board approved a new portfolio target allocation.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Notes to the Financial Statements, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**14. DEFINED BENEFIT PENSION PLAN (Continued)**

The target allocation and best estimates of real rates of return for each major asset class are summarized in the following table:

	Target Allocation	Long-Term Expected Real Rate of Return (Arithmetic)
Domestic Equity	17.5%	4.55%
International Equity	17.5%	6.10%
Core Fixed Income	10.0%	1.00%
Non-Core Fixed Income	20.0%	3.65%
Real Return	10.0%	4.03%
Real Estate	10.0%	5.00%
Absolute Return	10.0%	4.00%
Private Equity	5.0%	8.00%
Total	100.00%	

**Discount Rate:**

The discount rate used to measure the Total Pension Liability was (6.75%). The projection of cash flows used to determine the discount rate assumed that employee contributions will be made at the current 7% and employer contributions will be made at the rates specified in statute. Based on that assumption, the pension plan's Fiduciary Net Position was projected to be available to make all projected future benefit payments of current active and inactive employees. Therefore, the long-term expected rate of return on pension plan investments was applied to all periods of projected benefit payments to determine the Total Pension Liability.

**Sensitivity of the Net Pension Liability to Changes in the Discount Rate:**

The following presents the net pension liability of the System, calculated using the discount rate of (6.75%), as well as what the System's net pension liability would be if it were calculated using a discount rate that is 1 percentage point lower (5.75%) or 1 percentage point higher (7.75%) than the current rate:

	1% Decrease in Discount Rate (5.75%)	Current Discount Rate (6.75%)	1% Increase in Discount Rate (7.75%)
System's net pension liability (asset)	\$ 2,976,155	\$ 323,981	\$ (1,902,705)

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Notes to the Financial Statements, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**14. DEFINED BENEFIT PENSION PLAN (Continued)**

Changes in the Net Pension Liability:

	Total Pension Liability (a)	Increase/Decrease	
		Plan Fiduciary Net Pension (b)	Net Pension Liability (Asset) (a)-(b)
Balance at 12/31/2015	\$21,940,763	\$ 21,747,010	\$ 193,753
Changes for the year:			
Service cost	539,599	-	539,599
Interest (on Total Pension Liability)	1,453,483	-	1,453,483
Change of benefits terms	-	-	-
Difference between expected and actual experience	42,791	-	42,791
Changes of assumptions	-	-	-
Contributions - employer	-	35,295	(35,295)
Contributions - employee	-	418,757	(418,757)
Net investment income	-	1,469,085	(1,469,085)
Benefits payments, including refunds of employee contributions	(1,354,964)	(1,354,964)	-
Administrative expense	-	(16,598)	16,598
Other changes	-	(894)	894
Net changes	<u>\$ 680,909</u>	<u>\$ 550,681</u>	<u>\$ 130,228</u>
Balance at 12/31/2016	<u>\$22,621,672</u>	<u>\$ 22,297,691</u>	<u>\$ 323,981</u>

Changes in the Net Pension Liability:

	Total Pension Liability (a)	Increase/Decrease	
		Plan Fiduciary Net Pension (b)	Net Pension Liability (Asset) (a)-(b)
Balance at 12/31/2014	\$20,764,046	\$ 22,717,490	\$ (1,953,444)
Changes for the year:			
Service cost	487,964	-	487,964
Interest (on Total Pension Liability)	1,420,126	-	1,420,126
Change of benefits terms	-	-	-
Difference between expected and actual experience	130,618	-	130,618
Changes of assumptions	579,040	-	579,040
Contributions - employer	-	61,279	(61,279)
Contributions - employee	-	397,180	(397,180)
Net investment income	-	33,518	(33,518)
Benefits payments, including refunds of employee contributions	(1,441,031)	(1,441,031)	-
Administrative expense	-	(20,418)	20,418
Other changes	-	(1,008)	1,008
Net changes	<u>\$ 1,176,717</u>	<u>\$ (970,480)</u>	<u>\$ 2,147,197</u>
Balance at 12/31/2015	<u>\$21,940,763</u>	<u>\$ 21,747,010</u>	<u>\$ 193,753</u>

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Notes to the Financial Statements, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**14. DEFINED BENEFIT PENSION PLAN (Continued)**

Pension Plan Fiduciary Net Position:

Detailed information about the pension plan's Fiduciary Net Position is available in a separately-issued TMRS financial report. That report may be obtained on the Internet at [www.tmrs.com](http://www.tmrs.com).

Pension Expense and Deferred Outflows of Resources and Deferred Inflows of Resources Related to Pensions:

For the year ended September 30, 2017, the System recognized pension expense of \$627,961. This amount is included as part of Personnel Services expenses in the Statement of Revenues, Expenses and Changes in Net Position.

At September 30, 2017 and 2016, the System reported deferred outflows and deferred inflows of resources related to pensions from the following sources:

	<u>2017</u>		<u>2016</u>	
	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>	<u>Deferred Outflows of Resources</u>	<u>Deferred Inflows of Resources</u>
Pension contribution after the measurement date	\$ 80,713	\$ -	\$ 26,964	\$ -
Difference in projected and actual investment earnings	1,047,861	(930)	1,416,121	-
Difference in expected and actual pension experience	103,655	(55,526)	100,382	(93,042)
Changes in actuarial assumptions used to determine pension liability	310,966	-	445,003	-
	<u>\$ 1,543,195</u>	<u>\$ (56,456)</u>	<u>\$ 1,988,470</u>	<u>\$ (93,042)</u>

Deferred outflows of resources related to pensions resulting from contributions subsequent to the measurement date of \$80,713 will be recognized as a reduction of the net pension liability for the measurement year ending December 31, 2017(i.e. recognized in the System's financial statements as of September 30, 2018). Other amounts reported as deferred outflows and inflows of resources related to pensions will be recognized in pension expense as follows for 2017:

<u>Measurement Year Ended December 31</u>	
2017	\$ 504,067
2018	523,572
2019	372,958
2020	5,429
Total	<u>\$ 1,406,026</u>

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Notes to the Financial Statements, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**14. DEFINED BENEFIT PENSION PLAN (Continued)**

Deferred outflows and inflows of resources related to pensions from September 30, 2016 were to be amortized as follows:

Measurement Year Ended <u>December 31</u>		
2016	\$	495,017
2017		495,017
2018		514,522
2019		363,908
Total	\$	<u>1,868,464</u>

**15. OTHER POST EMPLOYMENT BENEFITS**

Supplemental Death Benefits Fund

The System participates in the cost sharing multiple-employer defined benefit group-term life insurance plan operated by the Texas Municipal Retirement System known as the Supplemental Death Benefits Fund (SDBF). The System elected, by resolution, to provide group-term life insurance coverage (Supplemental Death Benefits) to both current and retired employees. The System may terminate coverage under and discontinue participation in the SDBF by adopting a resolution before November 1 of any year to be effective the following January 1.

Benefits

Payments from this fund are similar to group-term life insurance benefits, and are paid to the designated beneficiaries upon the receipt of an approved application for payment. The death benefit for active employees provides a lump-sum payment approximately equal to the employee's annual salary (calculated based on the employee's actual earnings, for the 12-month period preceding the month of death). The death benefit for retirees is considered a postemployment benefit other than pension benefit (OPEB) and is a fixed amount of \$7,500. The obligations of this plan are payable only from the SDBF and are not an obligation of, or claim against, the pension trust fund.

Contributions

The System contributes to the SDBF at a contractually required rate as determined by an annual actuarial valuation. The rate is equal to the cost of providing one-year term life insurance. The funding policy for the SBDF program is to assure that adequate resources are available to meet all death benefit payments for the upcoming year; the intent is not to pre-fund retiree term life insurance during employees' entire careers.

The System's contributions to the TMRS SDBF for the fiscal years ended 2017, 2016, and 2015 were \$5,422, \$5,372, and \$4,468, respectively, which equaled the required contributions each year.

<u>Year</u>	Annual Required Contribution	Actual Contribution Made	Percentage of ARC
<u>Plan</u>	<u>(Rate)</u>	<u>(Rate)</u>	<u>Contributed</u>
2015	0.08%	0.08%	100.0%
2016	0.09%	0.09%	100.0%
2017	0.09%	0.09%	100.0%

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Notes to the Financial Statements, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**15. OTHER POST EMPLOYMENT BENEFITS (Continued)**

Retiree Health Care Plan

Plan Description

In addition to the pension benefits described in Note 14 and the supplemental death benefits described in Note 15, the System makes available health care and prescription-drug benefits to all employees who retire from the System and who are receiving benefits from the System sponsored retirement program, Texas Municipal Retirement System ("TMRS"). All current full-time employees of the System hired prior to February 2010 are eligible for retirement and health-care and prescription-drug coverage at age 60 with five years of service or at any age with 20 years of service. Those approved for disability retirement through TMRS are also eligible for retiree health-care and prescription-drug coverage. The System provided group health care coverage is discontinued at the end of the month prior to the retiree's 65<sup>th</sup> birth month. A Medicare Supplement, Plan F is provided thereafter, until death. The System provided health-care and prescription drug coverage and the Medicare Supplement premiums are paid 100% by the System.

Employees who are eligible for retirement, but instead choose to terminate employment, are not eligible for System sponsored health care and prescription drug coverage at a later date. Retirees who elect to opt-out of the System sponsored health care plan do not receive any cash payment in lieu of electing the System sponsored health care plan.

Spouses and dependents are eligible for COBRA coverage for 18 months (or up to 36 months under certain circumstances) following members retirement date. Spouse and dependent(s) are responsible for payment of the full premium amount. Retirees are required to enroll in Medicare once eligible. Retirees pay Medicare premiums. The System does not provide subsidized retiree vision or dental care coverage. Nor does the System provide subsidized retiree life insurance coverage. Life insurance coverage carried at the time of retirement is portable. The System does not provide a death-in-service benefit to a surviving spouse; however, through TMRS, there is a \$7,500 death benefit.

Funding Policy and Annual Retiree Health Care Plan Cost

The System's annual retiree health care plan cost is based upon the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement No. 45. The ARC represents a level of accrual that is projected to recognize the normal cost each year and to amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years. The System has not established a trust to fund the Retiree Health Care Plan liability and intends to continue the pay-as-you-go funding method. The System's Retiree Health Care Plan cost for the fiscal year ended September 30, is as follows:

	<u>2017</u>	<u>2016</u>
Annual required contribution (ARC)	\$ 690,905	\$ 726,557
Interest on Retiree Health Care Plan obligation	141,699	144,248
Adjustment to ARC	<u>(200,871)</u>	<u>(192,492)</u>
Annual Retiree Health Care Plan cost (expense) end of year	631,733	678,313
Estimated employer contribution	<u>(334,144)</u>	<u>(341,342)</u>
Increase in net Retiree Health Care Plan obligation	297,589	336,971
Net Retiree Health Care Plan obligation:		
As of beginning of the year	<u>3,542,478</u>	<u>3,205,507</u>
As of end of the year	<u>\$ 3,840,067</u>	<u>\$ 3,542,478</u>

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Notes to the Financial Statements, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**15. OTHER POST EMPLOYMENT BENEFITS (Continued)**

The System's annual Retiree Health Care Plan cost, the percentage of annual cost contributed to the plan, and the net obligation for the fiscal year ending September 30, 2017 and the two preceding fiscal years were as follows:

Fiscal Year Ended <u>September 30</u>	Annual OPEB <u>Cost</u>	Employer Amount <u>Contributed</u>	Percentage <u>Contributed</u>	Net OPEB <u>Obligations</u>
2015	\$ 683,882	\$ 313,880	45.9%	\$ 3,205,507
2016	678,313	341,342	50.3%	3,542,478
2017	631,733	334,144	52.9%	3,840,067

Funding Status and Funding Progress

The funded status of the System's retiree health care plan, under GASB Statement No. 45 as of September 30, 2017 and the two preceding fiscal years were as follows:

<u>Actuarial Valuation Date</u>	<u>Actuarial Value of Assets</u>	<u>Actuarial Accrued Liability (AAL)</u>	<u>Unfunded AAL (UAAL)</u>	<u>Funded Ratio</u>	<u>Annual Covered Payroll</u>	<u>Ratio of UAAL to Annual covered Payroll</u>
9/30/2015	\$ -	\$ 8,507,409	\$ 8,507,409	0.0%	\$ 5,584,459	152.3%
9/30/2016	-	8,507,409	8,504,409	0.0%	3,444,447	246.9%
9/30/2017	-	9,549,538	9,549,538	0.0%	3,209,168	297.6%

Under the reporting parameters, the System's retiree health care plan is 0.0% funded with an estimated actuarial accrued liability exceeding actuarial assets by \$9,549,538 at September 30, 2017. As of the most recent valuation, the ratio of the unfunded actuarial accrued liability to annual covered payroll is 297.6%.

Actuarial Methods and Assumptions

The Projected Unit Credit Cost Method is used to calculate the GASB ARC for the System's retiree health care plan. Using the plan benefits, the present health care premiums and a set of actuarial assumptions, the anticipated future payments are projected. The actuarial cost method then provides for a systematic funding for these anticipated payments. The yearly ARC is computed to cover the cost of benefits being earned by covered members as well as to amortize a portion of the unfunded accrued liability.

Projections of health benefits are based on the plan as understood by the System and include the types of benefits in force at the valuation date and the pattern of sharing benefit costs between the System and its employees to that point. Actuarial calculations reflect a long-term perspective and employ methods and assumptions that are designed to reduce short-term volatility in actuarial accrued liabilities and the actuarial value of assets.

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Notes to the Financial Statements, Continued**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

**15. OTHER POST EMPLOYMENT BENEFITS (Continued)**

Significant methods and assumptions were as follows:

	<u>Actuarial Methods and Assumptions</u>
Inflation rate	2.5% per annum
Investment rate of return	4.0% per annum, net of expenses
Actuarial cost method	Individual Entry Age Normal Cost Method
Amortization method	Level Dollar
Amortization period	30-year open amortization
Medical trend, Pre-65	Initial rate of 7.5% declining to an ultimate rate of 4.25% after 15 years
Medical trend, Post-65	Initial rate of 6.5% declining to an ultimate rate of 4.25% after 15 years

Actuarial valuations involve estimates of the value of reported amounts and assumptions about the probability of events in the future. Amounts determined regarding the funded status and the annual required contributions of the System's retiree health care plan are subject to continual revision as actual results are compared to past expectations and new estimates are made about the future. The required schedule of funding progress presented as required supplementary information provides multiyear trend information that shows whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

**16. DEFERRED COMPENSATION PLAN**

The System offers its employees a deferred compensation plan created in accordance with Internal Revenue Section 457. The plan, as amended, is available to all System employees, and permits them to defer a portion of their salary until future years. Participation in the plan is optional. The deferred compensation is not available to employees until termination, retirement, death, or unforeseeable emergency.

A 1996 federal law requires all assets and income of Internal Revenue Code 457 deferred compensation plans to be held in trust, custodial accounts, or annuity contracts for the exclusive benefit of the participants and their beneficiaries. Assets of the System's plan are administered by private corporations under contract with the City. Consequently, the plan's assets and liabilities are not reported in the System's financial statements.

**17. FUTURE FINANCIAL REPORTING REQUIREMENTS**

The System has reviewed GASB pronouncements which become effective in future years and notes the following statement is applicable to the System:

*Statement No. 75 Accounting and Financial reporting for Postemployment Benefits Other Than Pensions* – This statement changes the focus of accounting and postemployment benefits other than pensions from how much it costs to adequately fund the benefits over time to a point-in-time liability that is reflected on the employer's financial statements for any actuarially unfunded portion of benefits earned to date. This statement will become effective for the System in fiscal year 2018.

*Statement No. 84, Fiduciary Activities* – This statement establishes criteria for identifying fiduciary activities of governments and for identifying fiduciary component units and postemployment benefit arrangements that are fiduciary activities. This statement will become effective for the System in fiscal year 2020.

**REQUIRED SUPPLEMENTARY  
INFORMATION**

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Required Supplementary Information**

**Texas Municipal Retirement System**  
**Schedule of Changes in Net Pension Liability and Related Ratios**  
**Last Three Fiscal Years (Previous years are not available)**  
**(Unaudited)**

	Measurement Year Ended		
	12/31/2014	12/31/2015	12/31/2016
<b>Total pension liability:</b>			
Service Cost	\$ 457,206	\$ 487,964	\$ 539,599
Interest (on the total pension liability)	1,395,895	1,420,126	1,453,483
Changes of benefit terms	-	-	-
Difference between expected and actual experience	(168,074)	130,618	42,791
Changes of assumptions	-	579,040	-
Benefit payments, including refunds of employees contributions	(1,267,474)	(1,441,031)	(1,354,964)
Net change in total pension liability	\$ 417,553	\$ 1,176,717	\$ 680,909
Total pension liability - beginning	20,346,493	20,764,046	21,940,763
Total pension liability - ending	<u>\$ 20,764,046</u>	<u>\$ 21,940,763</u>	<u>\$ 22,621,672</u>
<b>Plan fiduciary net position:</b>			
Contributions - employer	\$ 114,431	\$ 61,279	\$ 35,295
Contributions - employee	381,436	397,180	418,757
Net investment income	1,271,634	33,518	1,469,085
Benefit payments, including refunds of employee contributions	(1,267,474)	(1,441,031)	(1,354,964)
Administrative expense	(13,278)	(20,418)	(16,598)
Other	(1,092)	(1,008)	(894)
Net change in plan fiduciary net position	\$ 485,657	\$ (970,480)	\$ 550,681
Plan fiduciary net position - beginning	22,231,833	22,717,490	21,747,010
Plan fiduciary net position - ending	<u>\$ 22,717,490</u>	<u>\$ 21,747,010</u>	<u>\$ 22,297,691</u>
Net pension liability (asset)	<u>\$ (1,953,444)</u>	<u>\$ 193,753</u>	<u>\$ 323,981</u>
Plan fiduciary net position as a percentage of the total pension liability	109.41%	99.12%	98.57%
Covered employee payroll	\$ 5,449,089	\$ 5,674,004	\$ 5,982,248
Net pension liability (asset) as a percentage of covered employee payroll	-35.85%	3.41%	5.42%

**CITY OF HARLINGEN WATERWORKS SYSTEM  
Required Supplementary Information**

**Texas Municipal Retirement System  
Schedule of Contributions  
Last Ten Fiscal Years  
(Unaudited)**

Fiscal Year	(1) Actuarially determined contribution	(2) Contribution in relation to the actuarially determined contribution	(3) Contribution excess (deficiency) (2)-(1)	(4) Covered employee payroll	(5) Actuarially determined contributions as a percentage of covered employee payroll (1)/(4)	(6) Contributions as a percent of coverage employee payroll (2)/(4)
2008	\$ 411,403	\$ 411,403	\$ -	\$ 4,281,201	9.61%	9.61%
2009	405,957	405,957	-	5,178,302	7.84%	7.84%
2010	353,893	353,893	-	5,030,408	7.04%	7.04%
2011	346,863	346,863	-	4,805,717	7.22%	7.22%
2012	198,737	198,737	-	4,916,937	4.04%	4.04%
2013	127,903	127,903	-	5,021,386	2.55%	2.55%
2014	117,027	117,027	-	5,261,273	2.22%	2.22%
2015	75,455	75,455	-	5,584,459	1.35%	1.35%
2016	43,964	43,964	-	6,144,250	0.72%	0.72%
2017	89,045	89,045	-	6,024,295	1.48%	1.48%

**Notes to Schedule of Contributions:**

**Valuation Date:**

Actuarially determined contribution rates are calculated as of December 31<sup>st</sup> and become effective in January, twelve months and a day later.

**Methods and Assumptions Used to Determine Contribution Rate for 2016:**

Actuarial Cost Method	Entry Age Normal
Amortization Method	Level Percentage of Payroll, Closed
Remaining Amortization Period	25 years
Asset Valuation Method	10 Year smoothed market; 15% soft corridor
Inflation	2.5%
Salary Increases	3.5% to 10.50% including inflation
Investment Rate of Return	6.75%
Retirement Age	Experience-based table of rates specific to the System's plan of benefits. Last updated for the 2015 valuation pursuant to an experience study of the period 2010-2014
Mortality	RP2000 Combined Mortality Table with Blue Collar Adjustment with male rates multiplied by 109% and female rates multiplied by 103% and projected on a fully generational basis with scale BB.

**Other Information:**

Notes There were no benefit changes during the year.

**CITY OF HARLINGEN WATERWORKS SYSTEM  
Required Supplementary Information**

**Texas Municipal Retirement System  
Schedule of Contributions  
Last Ten Fiscal years  
(Unaudited)**

Assumption differences for the fiscal years prior to 2017:

Actuarial Cost Method	Projected Unit Credit for fiscal years 2008 to 2013
Inflation	3% for fiscal years prior to 2017
Investment Rate of Return	7% for fiscal years prior to 2017
Mortality	Prior to fiscal year 2014, Gender Distinct RP2000 Combined Healthy Mortality Table projected to the year 2003 by scale AA

Other Information:

Fiscal years 2012 and forward include the impact of Senate Bill 350 enacted by the Texas Legislature in June 2011. This legislation provided a restructuring of the Texas Municipal Retirement System funds effective December 31, 2010. Previously reported amounts include only Employee Savings Fund and Municipal Accumulation Fund, but excluded the System's portion of the Current Service Annuity Fund (CSARF) in which costs for all retirees were shared. The legislation eliminated the CSARF returning both liabilities and assets for retirees to the respective employer accounts.

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**CITY OF HARLINGEN WATERWORKS SYSTEM  
Required Supplementary Information**

**Retiree Health Benefits Plan  
Schedule of Funding Progress  
Last Three Fiscal Years  
(Unaudited)**

Fiscal Year*	Actuarial Value of Assets	Actuarial Accrued Liability	Funded Ratio (1)/(2)	Unfunded		Annual Covered Payroll**	Unfunded Actuarial Accrued Liability As a Percentage of Covered Payroll
				Actuarial Accrued Liability	Annual Covered Payroll**		
2015	-	\$ 8,507,409	0.0%	\$ 8,507,409	\$ 5,584,459	152.34%	
2016	-	8,507,409	0.0%	8,507,409	3,444,447	246.99%	
2017	-	9,549,538	0.0%	9,549,538	3,209,168	297.57%	

\*As of September 30, 2017 actuarial valuation.

\*\* Annual covered payroll is the payroll related to those grandfathered employees who will be able to retire and continue health coverage.

**OTHER SUPPLEMENTARY  
INFORMATION**

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Schedule of Revenues, Expenses and Changes in Net Position**  
**Comparison of Actual to Budget**  
**For the Fiscal Year Ended September 30, 2017**

	Water		Percentage Variance	Wastewater		Percentage Variance
	Actual	Budget		Actual	Budget	
<b>Operating Revenue</b>						
Base charge	\$ 2,908,137	\$ 2,898,000	0.35%	\$ 1,673,551	\$ 1,662,600	0.66%
Service revenues	6,411,877	5,088,000	26.02%	8,201,718	7,545,000	8.70%
Sales to Combes	112,361	90,000	24.85%	215,684	175,000	23.25%
Sales to Primera	226,938	163,000	39.23%	124,069	155,000	-19.96%
Sales to Palm Valley	216,513	160,000	35.32%	-	-	-
Sales to East Rio Hondo	48,930	99,000	-50.58%	-	-	-
Sales to Military Highway	1,200	1,200	0.00%	-	-	-
Fuel adjustment	250,820	225,000	11.48%	242,169	225,000	7.63%
Customer penalties	161,866	120,000	34.89%	170,077	148,500	14.53%
Disconnect fees	195,435	185,000	5.64%	-	-	-
Industrial surcharge fees	-	-	0.00%	219,266	142,000	54.41%
Pretreatment testing fees	-	-	0.00%	15,444	14,400	7.25%
Other revenues	81,277	77,000	5.55%	125	-	-
Total operating revenues	<u>10,615,354</u>	<u>9,106,200</u>	16.57%	<u>10,862,103</u>	<u>10,067,500</u>	7.89%
<b>Operating expenses</b>						
Personnel services	4,511,248	4,675,766	-3.52%	3,664,438	3,629,374	0.97%
Contracted services	2,251,319	2,320,300	-2.97%	1,023,382	1,415,100	-27.68%
Supplies and maintenance	1,976,991	2,168,200	-8.82%	909,778	1,005,500	-9.52%
Other expenses	74,480	203,000	-63.31%	67,063	76,400	-12.22%
Depreciation expense	1,573,334	2,042,000	-22.95%	2,249,918	3,058,000	-26.43%
Total operating expenses	<u>10,387,372</u>	<u>11,409,266</u>	-8.96%	<u>7,914,579</u>	<u>9,184,374</u>	-13.83%
<b>Operating income (loss)</b>	<u>227,982</u>	<u>(2,303,066)</u>	-109.90%	<u>2,947,524</u>	<u>883,126</u>	233.76%
<b>Non-operating revenues</b>						
Impact fees	334,970	225,000	48.88%	433,260	265,000	63.49%
Investment earnings	104,762	37,500	179.37%	101,518	37,500	170.71%
Other revenues:						
Tap fees	69,475	60,000	15.79%	16,500	20,000	-17.50%
Inspection fees	4,251	2,000	112.55%	6,584	3,000	119.47%
Backflow prevention	27,025	21,000	28.69%	-	-	-
Tie in charges	16,648	18,000	-7.51%	16,947	9,000	88.30%
Rental income	64,834	64,500	0.52%	64,834	64,500	0.52%
Lease of water rights	151,483	-	-	-	-	-
Garbage billing fees	34,375	37,500	-8.33%	34,375	37,500	-8.33%
Work done for others	41,364	20,000	106.82%	6,655	3,000	121.83%
Gain(loss) on disposition of assets	13,579	20,000	-32.11%	(220,646)	10,000	-2306.46%
Other revenue	41,147	30,000	37.16%	119,849	100,000	19.85%
Total non-operating revenue	<u>903,913</u>	<u>535,500</u>	68.80%	<u>579,876</u>	<u>549,500</u>	5.53%
<b>Non-operating expenses</b>						
Interest and amortization expense	<u>326,510</u>	<u>424,226</u>	-23.03%	<u>329,936</u>	<u>427,361</u>	-22.80%
<b>Change in net position before contributions</b>	<u>805,385</u>	<u>(2,191,792)</u>	-136.75%	<u>3,197,464</u>	<u>1,005,265</u>	218.07%
Capital contributions	<u>204,131</u>	<u>-</u>	100.00%	<u>228,751</u>	<u>-</u>	100%
<b>Change in net position</b>	<u>\$ 1,009,516</u>	<u>\$ (2,191,792)</u>	-146.06%	<u>\$ 3,426,215</u>	<u>\$ 1,005,265</u>	240.83%

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Schedule of Revenues, Expenses and Changes in Net Position**  
**Comparison of Actual to Budget**  
**For the Fiscal Year Ended September 30, 2017**

	Total		Percentage Variance
	Actual	Budget	
<b>Operating Revenue</b>			
Base charge	\$ 4,581,688	\$ 4,560,600	0.46%
Service revenues	14,613,595	12,633,000	15.68%
Sales to Combes	328,045	265,000	23.79%
Sales to Primera	351,007	318,000	10.38%
Sales to Palm Valley	216,513	160,000	35.32%
Sales to East Rio Hondo	48,930	99,000	-50.58%
Sales to Military Highway	1,200	1,200	-
Fuel adjustment	492,989	450,000	9.55%
Customer penalties	331,943	268,500	23.63%
Disconnect fees	195,435	185,000	5.64%
Industrial surcharge fees	219,266	142,000	54.41%
Pretreatment testing fees	15,444	14,400	7.25%
Other revenues	81,402	77,000	5.72%
Total operating revenues	<u>21,477,457</u>	<u>19,173,700</u>	12.02%
<b>Operating expenses</b>			
Personnel services	8,175,686	8,305,140	-1.56%
Contracted services	3,274,701	3,735,400	-12.33%
Supplies and maintenance	2,886,769	3,173,700	-9.04%
Other expenses	141,543	279,400	-49.34%
Depreciation expense	3,823,252	5,100,000	-25.03%
Total operating expenses	<u>18,301,951</u>	<u>20,593,640</u>	-11.13%
<b>Operating income (loss)</b>	<u>3,175,506</u>	<u>(1,419,940)</u>	-323.64%
<b>Non-operating revenues</b>			
Impact fees	768,230	490,000	56.78%
Investment earnings	206,280	75,000	175.04%
Other revenues:			
Tap fees	85,975	80,000	7.47%
Inspection fees	10,835	5,000	116.70%
Backflow prevention	27,025	21,000	28.69%
Tie in charges	33,595	27,000	24.43%
Rental income	129,668	129,000	0.52%
Lease of water rights	151,483	-	-
Garbage billing fees	68,750	75,000	-8.33%
Work done for others	48,019	23,000	108.78%
Gain(loss) on disposition of assets	(207,067)	30,000	-790.22%
Other revenue	160,996	130,000	23.84%
Total non-operating revenue	<u>1,483,789</u>	<u>1,085,000</u>	36.75%
<b>Non-operating expenses</b>			
Interest and amortization expense	656,446	851,587	-22.91%
<b>Change in net position before contributions</b>	4,002,849	(1,186,527)	-437.36%
Capital contributions	432,882	-	100.00%
<b>Change in net position</b>	<u>\$ 4,435,731</u>	<u>\$ (1,186,527)</u>	-473.84%

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Schedule of Revenues, Expenses and Changes in Net Position**  
**Water, Wastewater and Total System**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

	Water		Percentage Variance	Wastewater		Percentage Variance
	2017	2016		2017	2016	
<b>Operating Revenue</b>						
Base charge	\$ 2,908,137	\$ 2,871,617	1.27%	\$ 1,673,551	\$ 1,365,929	22.52%
Service revenues	6,411,877	5,331,929	20.25%	8,201,718	7,756,792	5.74%
Sales to Combes	112,361	98,730	13.81%	215,684	231,169	-6.70%
Sales to Primera	226,938	194,439	16.71%	124,069	157,701	-21.33%
Sales to Palm Valley	216,513	184,711	17.22%	-	-	-
Sales to East Rio Hondo	48,930	4,377	1017.89%	-	-	-
Sales to Military Highway	1,200	1,200	0.00%	-	-	-
Fuel adjustment	250,820	243,445	3.03%	242,169	229,141	5.69%
Customer penalties	161,866	132,647	22.03%	170,077	156,279	8.83%
Disconnect fees	195,435	196,980	-0.78%	-	-	-
Industrial surcharge fees	-	-	-	219,266	172,778	26.91%
Pretreatment testing fees	-	-	-	15,444	14,683	5.18%
Other revenues	81,277	78,730	3.24%	125	-	0.00%
Total operating revenues	<u>10,615,354</u>	<u>9,338,805</u>	13.67%	<u>10,862,103</u>	<u>10,084,472</u>	7.71%
<b>Operating expenses</b>						
Personnel services	4,511,248	4,545,077	-0.74%	3,664,438	3,506,213	4.51%
Contracted services	2,251,319	2,147,850	4.82%	1,023,382	1,311,616	-21.98%
Supplies and maintenance	1,976,991	2,017,205	-1.99%	909,778	920,009	-1.11%
Other expenses	74,480	125,206	-40.51%	67,063	115,259	-41.82%
Depreciation expense	1,573,334	2,177,914	-27.76%	2,249,918	2,824,311	-20.34%
Total operating expenses	<u>10,387,372</u>	<u>11,013,252</u>	-5.68%	<u>7,914,579</u>	<u>8,677,408</u>	-8.79%
<b>Operating income (loss)</b>	<u>227,982</u>	<u>(1,674,447)</u>	-113.62%	<u>2,947,524</u>	<u>1,407,064</u>	109.48%
<b>Non-operating revenues</b>						
Impact fees	334,970	207,695	61.28%	433,260	256,681	68.79%
Investment earnings	104,762	59,421	76.30%	101,518	58,075	74.80%
Other revenues:						
Tap fees	69,475	55,400	25.41%	16,500	14,475	13.99%
Inspection fees	4,251	1,902	123.50%	6,584	3,987	65.14%
Backflow prevention	27,025	21,360	26.52%	-	-	0.00%
Tie in charges	16,648	28,011	-40.57%	16,947	11,343	49.40%
Lease of water rights	151,483	-	0.00%	-	-	-
Rental income	64,834	67,371	-3.77%	64,834	67,371	-3.77%
Garbage billing fees	34,375	37,500	-8.33%	34,375	37,500	-8.33%
Work done for others	41,364	32,864	25.86%	6,655	8,808	-24.44%
Gain(loss) on disposition of assets	13,579	19,613	-30.77%	(220,646)	3,967	-5662.04%
Other revenue	41,147	34,708	18.55%	119,849	134,364	-10.80%
Total non-operating revenue	<u>903,913</u>	<u>565,845</u>	59.75%	<u>579,876</u>	<u>596,571</u>	-2.80%
<b>Non-operating expenses</b>						
Interest and amortization expense	326,510	306,005	6.70%	329,936	308,878	6.82%
<b>Change in net position before contributions</b>	805,385	(1,414,607)	-156.93%	3,197,464	1,694,757	88.67%
Capital contributions	204,131	112,608	81.28%	228,751	106,802	114.18%
<b>Change in net position</b>	<u>\$ 1,009,516</u>	<u>\$ (1,301,999)</u>	-177.54%	<u>\$ 3,426,215</u>	<u>\$ 1,801,559</u>	90.18%

**CITY OF HARLINGEN WATERWORKS SYSTEM**  
**Schedule of Revenues, Expenses and Changes in Net Position**  
**Water, Wastewater and Total System**  
**For the Fiscal Years Ended September 30, 2017 and 2016**

	Total		Percentage Variance
	2017	2016	
<b>Operating Revenue</b>			
Base charge	\$ 4,581,688	\$ 4,237,546	8.12%
Service revenues	14,613,595	13,088,721	11.65%
Sales to Combes	328,045	329,899	-0.56%
Sales to Primera	351,007	352,140	-0.32%
Sales to Palm Valley	216,513	184,711	17.22%
Sales to East Rio Hondo	48,930	4,377	1017.89%
Sales to Military Highway	1,200	1,200	0.00%
Fuel adjustment	492,989	472,586	4.32%
Customer penalties	331,943	288,926	14.89%
Disconnect fees	195,435	196,980	-0.78%
Industrial surcharge fees	219,266	172,778	26.91%
Pretreatment testing fees	15,444	14,683	5.18%
Other revenues	81,402	78,730	3.39%
Total operating revenues	<u>21,477,457</u>	<u>19,423,277</u>	10.58%
<b>Operating expenses</b>			
Personnel services	8,175,686	8,051,290	1.55%
Contracted services	3,274,701	3,459,466	-5.34%
Supplies and maintenance	2,886,769	2,937,214	-1.72%
Other expenses	141,543	240,465	-41.14%
Depreciation expense	3,823,252	5,002,225	-23.57%
Total operating expenses	<u>18,301,951</u>	<u>19,690,660</u>	-7.05%
<b>Operating income (loss)</b>	<u>3,175,506</u>	<u>(267,383)</u>	-1287.62%
<b>Non-operating revenues</b>			
Impact fees	768,230	464,376	65.43%
Investment earnings	206,280	117,496	75.56%
Other revenues:			
Tap fees	85,975	69,875	23.04%
Inspection fees	10,835	5,889	83.99%
Backflow prevention	27,025	21,360	26.52%
Tie in charges	33,595	39,354	-14.63%
Lease of water rights	151,483	-	-
Rental income	129,668	134,742	-3.77%
Garbage billing fees	68,750	75,000	-8.33%
Work done for others	48,019	41,672	15.23%
Gain(loss) on disposition of assets	(207,067)	23,580	-978.15%
Other revenue	160,996	169,072	-4.78%
Total non-operating revenue	<u>1,483,789</u>	<u>1,162,416</u>	27.65%
<b>Non-operating expenses</b>			
Interest and amortization expense	<u>656,446</u>	<u>614,883</u>	6.76%
<b>Change in net position before contributions</b>	4,002,849	280,150	1328.82%
Capital contributions	<u>432,882</u>	<u>219,410</u>	97.29%
<b>Change in net position</b>	<u>\$ 4,435,731</u>	<u>\$ 499,560</u>	787.93%

# **STATISTICAL SECTION**

**CITY OF HARLINGEN WATERWORKS SYSTEM  
SCHEDULE OF REVENUE BOND COVERAGE  
Last Ten Fiscal Years**

Fiscal Year	Gross Revenues	(1) Operating Expenses	Net Revenue Available for Debt Service (2)	Annual Debt Service Requirement			(3) Coverage Ratio
				Principal	Interest	Total	
2008	\$ 19,171,341	\$ 13,117,892	\$ 6,053,449	\$ 1,645,000	\$ 735,577	\$ 2,380,577	2.54
2009	20,014,422	14,662,383	5,352,039	1,695,000	692,686	2,387,686	2.24
2010	17,374,281	12,771,254	4,603,027	2,120,000	632,608	2,752,608	1.67
2011	20,185,415	12,785,464	7,399,951	1,850,000	738,190	2,588,190	2.86
2012	20,802,973	13,098,103	7,704,870	1,910,000	688,990	2,598,990	2.96
2013	20,337,489	13,504,156	6,833,333	1,980,000	629,890	2,609,890	2.62
2014	19,132,562	13,804,689	5,327,873	900,000	582,309	1,482,309	3.56
2015	18,770,642	13,801,280	4,969,362	320,000	576,203	896,203	5.54
2016	20,585,693	14,688,435	5,897,258	1,455,000	787,781	2,242,781	2.63
2017	22,961,246	14,478,699	8,482,547	1,480,000	757,606	2,237,606	3.79

(1) All operating and non-operating revenues of the System.

(2) Expenses of operation and maintenance of the System, including salaries, labor, materials, repairs and extensions necessary to render efficient service. Depreciation and payments into and out of the interest and sinking fund and the reserve fund are excluded.

(3) The debt service due within one year of the fiscal year end.

**CITY OF HARLINGEN WATERWORKS SYSTEM  
NUMBER OF CONNECTIONS  
Last Ten Fiscal Years**

WATER SYSTEM			
Fiscal Year	Active Connections	Inactive Connections	Total Connections
2008	23,830	3,229	27,059
2009	23,446	3,774	27,220
2010	23,824	3,668	27,492
2011	24,144	3,611	27,755
2012	24,445	3,523	27,968
2013	24,592	2,766	27,358
2014	24,842	2,754	27,596
2015	25,087	2,728	27,815
2016	25,248	2,835	28,083
2017	25,624	2,789	28,413

WASTEWATER SYSTEM			
Fiscal Year	Active Connections	Inactive Connections	Total Connections
2008	18,821	4,099	22,920
2009	18,978	3,419	22,397
2010	19,226	3,187	22,413
2011	19,457	3,083	22,540
2012	19,633	3,012	22,645
2013	19,762	2,976	22,738
2014	19,687	2,900	22,587
2015	19,892	1,582	21,474
2016	20,013	1,622	21,635
2017	20,164	928	21,092

**CITY OF HARLINGEN WATERWORKS SYSTEM  
MONTHLY WATER RATES (Effective October 1, 2017)**

**Base Rate: Residential and Commercial**

Meter Size	Inside City Limits	Outside City Limits
3/4"	\$ 7.93	\$ 12.49
1"	10.07	15.09
1 1/2"	14.56	21.86
2"	33.02	49.55
3"	49.17	73.77
4"	112.87	169.32
6"	231.80	346.97
8"	426.15	639.24

**Commodity Charge**

(per each 1,000 gallons of water usage)

All meters	\$ 1.65	\$ 2.48
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**Fuel Cost Adjustment**

(per each 1,000 gallons of water usage)

All meters	\$ 0.06	\$ 0.06
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**Monthly Fire Suppression Charge**

Meter Size	
4"	\$ 5.00
6"	7.00
8"	9.00
10"	11.00
12"	13.00

**CITY OF HARLINGEN WATERWORKS SYSTEM  
MONTHLY SEWER RATES (Effective October 1, 2017)**

**Base Rate: Residential and Commercial**

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Meter Size	Inside City Limits	Outside City Limits
3/4"	\$ 5.78	\$ 20.10
1"	9.04	20.10
1 1/2"	21.01	21.01
2"	25.37	25.37
3"	52.57	52.57
4"	134.20	134.20
6"	275.68	275.68
8"	438.93	438.93

**Commodity Charge**

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All meters	\$ 3.66	\$ 3.66
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**Fuel Cost Adjustment**

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All meters	\$ 0.11	\$ 0.11
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**CITY OF HARLINGEN WATERWORKS SYSTEM  
TOP TEN WATER CUSTOMERS**

<u>Customer</u>	<u>Type of Industry</u>	<u>Water Revenues</u>	<u>% of Total</u>	<u>Water Used (in thousands)</u>	<u>% of Total</u>
Harlingen C.I.S.D.	Education	\$ 306,374	2.89%	161,927	3.97%
City of Primera	Municipality	226,938	2.14%	133,703	3.28%
City of Palm Valley	Municipality	216,512	2.04%	127,580	3.13%
Valley Baptist Medical Center	Health Care	156,491	1.47%	86,425	2.12%
City of Combes	Municipality	129,484	1.22%	98,511	2.41%
Paradise Park	Mobile Home Park/Housing	108,485	1.02%	64,110	1.57%
Harlingen Medical Center	Health Care	49,337	0.46%	28,154	0.69%
East Rio Hondo Water Supply	Water Supplier	48,930	0.46%	28,090	0.69%
Texas State Technical College	Higher Education	46,770	0.44%	22,165	0.54%
Mexican Snacks	Food Processing	43,493	0.41%	16,107	0.39%
		<b><u>\$ 1,332,814</u></b>	<b><u>12.55%</u></b>	<b><u>766,772</u></b>	<b><u>18.79%</u></b>
	<b>Total Revenues/Gallons</b>	<b>\$ 10,615,354</b>		<b>4,080,700</b>	

**CITY OF HARLINGEN WATERWORKS SYSTEM  
TOP TEN SEWER CUSTOMERS**

<u>Customer</u>	<u>Type of Industry</u>	<u>Sewer Revenues</u>	<u>% of Total</u>
Valley Baptist Medical Center	Health Care	\$ 269,765	2.48%
Harlingen C.I.S.D	Education	241,112	2.22%
City of Combes	Municipality	231,563	2.13%
Paradise Park	Mobile Home Park/Housing	202,182	1.86%
City of Primera	Municipality	132,385	1.22%
Harlingen Medical Center	Health Care	95,595	0.88%
Texas Industrial Service	Laundry/Uniform Service	83,778	0.77%
Valco Chemical Co.	Industrial	82,778	0.76%
East Rio Hondo Water Supply	Rural Water Supply	70,720	0.65%
Texas State Technical College	Higher Education	68,451	0.63%
		<b><u>\$ 1,478,329</u></b>	<b><u>13.60%</u></b>
	<b>Total Wastewater Revenue</b>	<b>\$10,862,103</b>	

**CITY OF HARLINGEN WATERWORKS SYSTEM  
HISTORICAL WATER PUMPAGE VOLUME - RAW WATER**

<b>Fiscal Year Ended 9/30</b>	<b>Daily Average (millions)</b>	<b>Peak Day (millions)</b>	<b>Peak Month (millions)</b>	<b>Total Annual Usage (millions)</b>	<b>Paid To Irrigation District</b>
2008	13.4	21.0	493.4	4,896.9	\$ 804,733
2009	14.0	24.1	600.3	5,139.2	813,168
2010	11.6	20.3	429.7	4,643.2	673,276
2011	13.6	20.5	530.7	4,961.4	839,973
2012	14.1	23.6	543.7	5,156.6	956,142
2013	13.9	20.5	484.4	5,079.7	1,052,773
2014	12.9	21.1	561.6	4,709.0	991,612
2015	12.0	22.0	520.1	4,376.5	1,010,833
2016	13.2	22.2	561.4	4,838.9	1,154,384
2017	14.1	20.6	517.0	5,143.0	1,214,127

**CITY OF HARLINGEN WATERWORKS SYSTEM  
HISTORICAL WATER PUMPAGE VOLUME - HIGH SERVICE**

<b>Fiscal Year Ended 9/30</b>	<b>Daily Average (millions)</b>	<b>Peak Day (millions)</b>	<b>Peak Month (millions)</b>	<b>Total Annual Usage (millions)</b>	<b>Water Revenue</b>
2008	12.5	19.8	467.4	4,587.5	\$8,279,977
2009	13.1	20.3	545.5	4,788.3	8,775,579
2010	10.3	14.8	379.2	3,761.2	7,465,844
2011	13.0	17.1	503.1	4,733.9	9,026,782
2012	13.3	23.6	503.5	4,878.5	9,274,968
2013	13.1	19.7	453.7	4,786.9	8,873,457
2014	12.0	20.4	541.7	4,393.4	8,288,521
2015	11.6	20.7	513.2	4,230.5	8,255,106
2016	12.9	22.5	549.2	4,724.5	9,338,805
2017	13.9	19.9	499.0	5,058.0	10,615,354

**CITY OF HARLINGEN WATERWORKS SYSTEM  
HISTORICAL WASTEWATER TREATMENT VOLUME**

<b>Fiscal Year Ended 9/30</b>	<b>Daily Average (millions)</b>	<b>Monthly Average (millions)</b>	<b>Total Annual Usage (millions)</b>	<b>Sewer Revenue</b>
2008	6.6	202.3	2,427.2	\$8,479,660
2009	6.4	193.5	2,321.7	9,304,795
2010	6.2	189.5	2,274.6	8,835,245
2011	6.2	189.7	2,276.4	10,109,783
2012	5.8	175.6	2,107.0	10,332,777
2013	5.7	171.8	2,061.4	10,009,046
2014	5.8	174.9	2,099.0	9,431,250
2015	6.1	186.7	2,240.1	9,329,251
2016	6.0	182.9	2,378.3	10,084,472
2017	5.6	168.8	2,026.0	10,862,103

# **COMPLIANCE SECTION**

**INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL  
OVER FINANCIAL REPORTING AND ON COMPLIANCE AND  
OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL  
STATEMENTS PERFORMED IN ACCORDANCE WITH  
GOVERNMENT AUDITING STANDARDS**

To the City of Harlingen  
Waterworks System Board of Trustees

We have audited, in accordance with the auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the City of Harlingen Waterworks System, as of and for the year ended September 30, 2017, and the related notes to the financial statements, which collectively comprise the City of Harlingen Waterworks System's basic financial statements, and have issued our report thereon dated March 28, 2018.

**Internal Control over Financial Reporting**

In planning and performing our audit of the financial statements, we considered the City of Harlingen Waterworks System's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the City of Harlingen Waterworks System's internal control. Accordingly, we do not express an opinion on the effectiveness of the City of Harlingen Waterworks System's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or, significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

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## **Compliance and Other Matters**

As part of obtaining reasonable assurance about whether the City of Harlingen Waterworks System's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

## **Purpose of this Report**

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

*Carr, Riggs & Ingram, L.L.C.*

Harlingen, Texas  
March 28, 2018